

# SHAPING A SUSTAINABLE FINANCIAL SYSTEM

Future-proofing global finance for a net-zero, nature-positive world

EU



# OVERVIEW

By 2030, the EU seeks to reduce greenhouse gas (GHG) emissions by

**55%**  
(compared to 1990 levels)

GHG emissions in the EU reduced by

**24%**  
between 1990 and 2019

**By 2030, the EU seeks to reduce greenhouse gas (GHG) emissions by 55% (compared to 1990 levels) as well as addressing biodiversity, deforestation and water security issues as part of the European Green Deal (EGD), a framework for the environmental and climate transition in the EU. By 2050, climate neutrality is to be achieved<sup>1</sup>.**

With GHG emissions in the EU reduced by 24% between 1990 and 2019, the EU is overshooting its 2020 climate target of 20%<sup>2</sup>. However, to reach its 2030 target, more ambitious action is needed. Since Art. 2.1°c of the Paris Agreement lifted finance higher on the international agenda of climate action, sustainable finance has become a key pillar of EU climate policy. To achieve emission reductions of 40% by 2030 (the previous 2030 climate target), EUR 180 billion in additional investments would be required annually<sup>3</sup>. Under the EGD, the EU seeks to mobilise at least EUR 1 trillion of sustainable investments over the next decade<sup>4</sup>.

This financing gap is addressed by the sustainable finance policy agenda in the EU.

The **Action Plan on Financing Sustainable Growth**, adopted in March 2018, put forward ten measures to drive financial institutions to shift capital flows towards the low-carbon transition of business practices. Two key policy components that are critical to achieving this shift are the EU Taxonomy and transparency and disclosure requirements<sup>5</sup>. With the **Renewed Sustainable Finance Strategy**, published July 2021, the EU renewed its commitment to sustainable finance and seeks to strengthen the policy framework. The renewed agenda addresses four gaps: providing tools to address the transition; catering to the needs of SMEs; addressing the financial sector's double materiality; and fostering consensus for a global sustainable finance agenda.



1. European Commission: Climate Action. 2030 climate & energy framework, [https://ec.europa.eu/clima/policies/strategies/2030\\_en](https://ec.europa.eu/clima/policies/strategies/2030_en); European Commission: Climate Action. 2050 long-term strategy, [https://ec.europa.eu/clima/policies/strategies/2050\\_en](https://ec.europa.eu/clima/policies/strategies/2050_en)
2. European Commission: Climate Action. Progress made in cutting emissions, [https://ec.europa.eu/clima/policies/strategies/progress\\_en](https://ec.europa.eu/clima/policies/strategies/progress_en)
3. European Commission: Factsheet: Financing sustainable growth, [https://ec.europa.eu/info/sites/default/files/business\\_economy\\_euro/banking\\_and\\_finance/documents/finance-events-190321-factsheet\\_en\\_0.pdf](https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/finance-events-190321-factsheet_en_0.pdf)
4. European Commission: Overview of sustainable finance, [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance_en)
5. European Commission: Factsheet: Financing sustainable growth, [https://ec.europa.eu/info/sites/default/files/business\\_economy\\_euro/banking\\_and\\_finance/documents/finance-events-190321-factsheet\\_en\\_0.pdf](https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/finance-events-190321-factsheet_en_0.pdf)

# KEY SUSTAINABLE FINANCE POLICY ACTORS

The EU's sustainable finance agenda has encompassed an extensive group of policy actors with direct or indirect contribution to the policy making process.

European Institutions	Responsibilities and actions taken
EUROPEAN COMMISSION (EC)	Presents legislative proposals under the co-decision (COD) procedure.
EUROPEAN PARLIAMENT (EP)	The COD procedure empowers the EP and the Council with the prerogative to scrutinise the proposal text.
COUNCIL OF THE EU (THE COUNCIL)	
COMMITTEES	Committees in both institutions amend and vote on the proposals before proceeding to tripartite negotiations between the EC, EP and the Council.
Once a provisional agreement is reached on the finalised text, the text passes through the formal approval procedures in both the EP and the Council before the acts are formally adopted <sup>6</sup> .	
EUROPEAN REGULATORS AND SUPERVISORS	
EUROPEAN SYSTEM OF FINANCIAL SUPERVISION (ESFS)	The framework within which the supervision of the financial market is located, including the European Systemic Risk Board (ESRB), the independent <b>European Supervisory Authorities</b> (ESA's, namely the EBA <sup>7</sup> , ESMA <sup>8</sup> and EIOPA <sup>9</sup> ) and national supervisory authorities. The main objectives of these supervisors in the respective fields are financial stability and the implementation of standards and rulebooks deriving from legislation <sup>10</sup> .
EUROPEAN SECURITIES AND MARKETS AUTHORITY (ESMA),	The main implementing body of the sustainable finance agenda covering amongst others the areas of ESG, environmental disclosure and climate benchmarks. In addition to taking an active role in public consultations on legislative files by the EU, ESMA supports shaping the technical aspects of policy in the financial market. In February 2020, ESMA published its sustainable finance strategy. Four key areas are addressed as its areas of work on the topic: further and harmonise the framework on transparency/disclosures; ensure consistency of guidelines and among national implementation by national authorities; assess the risks from developments in sustainable finance (especially in regards to green bonds); and collaborate and communicate with stakeholders <sup>12</sup> . As part of this, ESMA proposed Regulatory Technical Standards (RTS) as guidelines for product-related disclosure under the taxonomy and respectively the SFRD <sup>13</sup> . ESMA is also participating in the <b>EU Platform on Sustainable Finance</b> <sup>14</sup> .

6. European Parliament: Interinstitutional negotiations for the adoption of EU legislation: <https://www.europarl.europa.eu/olp/en/interinstitutional-negotiations>

7. European Banking Authority (EBA)

8. European Securities and Markets Authority (ESMA)

9. European Insurance and Occupational Pensions Authority (EIOPA)

10. European Parliament: Fact Sheets on the European Union, European System of Financial Supervision (ESFS), <https://www.europarl.europa.eu/factsheets/en/sheet/84/european-system-of-financial-supervision-esfs>

11. ESMA: ESMA's role, <https://www.esma.europa.eu/policy-activities/sustainable-finance/esma%E2%80%99s-role>

12. ESMA: ESMA sets out its strategy on sustainable finance, Press release, 06 February 2020, <https://www.esma.europa.eu/press-news/esma-news/esma-sets-out-its-strategy-sustainable-finance>; ESMA: Strategy on Sustainable Finance, ESMA22-105-1052, [https://www.esma.europa.eu/sites/default/files/library/esma22-105-1052\\_sustainable\\_finance\\_strategy.pdf](https://www.esma.europa.eu/sites/default/files/library/esma22-105-1052_sustainable_finance_strategy.pdf)

13. ESMA: Joint Consultation on Taxonomy-related Sustainability Disclosures, <https://www.esma.europa.eu/press-news/consultations/joint-consultation-taxonomy-related-sustainability-disclosures>

14. ESMA: ESMA sets out its strategy on sustainable finance, Press release, 06 February 2020, <https://www.esma.europa.eu/press-news/esma-news/esma-sets-out-its-strategy-sustainable-finance>

European Institutions	Responsibilities and actions taken
<b>EXPERT AND ADVISORY GROUPS</b>	
<b>HIGH-LEVEL EXPERT GROUP (HLEG)</b>	<p>In 2016, the EC established a <b>High-level expert group (HLEG)</b> on sustainable finance, which was comprised of 20 senior experts from civil society organisations, academia and industry<sup>15</sup>. The group advised the EC on sustainable investments, financial stability and policy deployment and published its final report in 2018; the findings of which contributed to the European Parliament’s Sustainable Finance own initiative report in 2018<sup>16</sup>,</p>
<b>TECHNICAL EXPERT GROUP ON SUSTAINABLE FINANCE (TEG)</b>	<p>In the process of forming its legislative proposals, the EC appointed a <b>Technical Expert Group on Sustainable Finance (TEG)</b> tasked with advising on diverse aspects of implementation<sup>17</sup>. With sustainable finance legislation resulting from the action plan in place since 2020, the work by the TEG was concluded and the Platform on Sustainable Finance took its place.</p>
<b>EU PLATFORM ON SUSTAINABLE FINANCE<sup>18</sup></b>	<p>Appointed by the EC, the Platform is a permanent advisory group consisting of public and private experts (from business, the public sector, academia and civil society) tasked with developing the technical criteria for implementation of the EU Taxonomy and ensuring sustainable objectives of the EU Taxonomy are met. It also expands beyond this, advising on sustainable finance policy and supporting the delivery of the EGD and the EU climate targets<sup>19</sup>.</p> <p>Advises the EC on amendments to legislation, such as technical criteria for the taxonomy<sup>20</sup>.</p>
<b>EUROPEAN FINANCIAL REPORTING ADVISORY GROUP (EFRAG)</b>	<p>An independent private association: in 2020, the EC tasked EFRAG with starting preparatory work on the world’s first public standards for sustainability reporting<sup>21</sup>. These standards will be vital for delivering the EU’s ambitious environmental and sustainable finance agenda. They will power the Corporate Sustainability Reporting Directive, and improve the relevance, completeness, and decision-usefulness of the data companies report by law. The first disclosures using the standards will be filed in 2023.</p> <p>Specific project task forces are established by EFRAG, comprised of a multistakeholder platform, which carries out technical work on climate-related reporting, sustainability and non-financial reporting standards.</p>
<b>OTHER POLICY ACTORS</b>	
<p>On an EU and Member State level, there are a large variety of associations and organisations involved in the sustainable finance debate. As per the Aarhus Convention, ‘public participation in environmental decision-making’ must be ensured<sup>22</sup>. Thus, sustainable finance legislation is subject to public consultation and other forms of stakeholder engagement. Business, civil society and academic organisations as well as national institutions can formally provide responses to the legislative proposals, which may be taken into account by the EC. All sustainable finance legislative proposals undergo this public consultation process, such as, in 2020, when the EC launched its renewed sustainable finance strategy<sup>23</sup> with a public consultation, inviting all citizens, Member States and organisations to share their views on the EU’s renewed sustainable finance agenda. The responses to this public consultation were summarised in a <a href="#">report</a> published by the EC in February 2021.</p>	

**Nb: This is not an exhaustive list of actors but key regulatory and institutional bodies in the EU’s strategy on greening the financial system**

15. European Commission: High-level expert group on sustainable finance (HLEG): [https://ec.europa.eu/info/publications/sustainable-finance-high-level-expert-group\\_en](https://ec.europa.eu/info/publications/sustainable-finance-high-level-expert-group_en)

16. European Parliament: resolution of 29 May 2018 on sustainable finance (2018/2007(INI)): [https://www.europarl.europa.eu/doceo/document/TA-8-2018-0215\\_EN.pdf](https://www.europarl.europa.eu/doceo/document/TA-8-2018-0215_EN.pdf)

17. European Commission: Technical expert group on sustainable finance (TEG), 13 June 2018 (last update on: 15 July 2020), [https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group\\_en](https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en)

18. ESMA: ESMA sets out its strategy on sustainable finance, Press release, 06 February 2020, <https://www.esma.europa.eu/press-news/esma-news/esma-sets-out-its-strategy-sustainable-finance>

19. European Commission: Platform on sustainable finance. The platform is an advisory body subject to the Commission’s horizontal rules for expert groups, [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance/platform-sustainable-finance\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance/platform-sustainable-finance_en)

20. European Commission: Platform on sustainable finance. The platform is an advisory body subject to the Commission’s horizontal rules for expert groups, [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance/platform-sustainable-finance\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance/platform-sustainable-finance_en)

21. <https://www.efrag.org/News/Project-476/Reports-published-on-development-of-EU-sustainability-reporting-standards>

22. European Commission: Environment. Aarhus Convention, <https://ec.europa.eu/environment/aarhus/>

23. European Commission: Renewed sustainable finance strategy and implementation of the action plan on financing sustainable growth: [https://ec.europa.eu/info/publications/sustainable-finance-renewed-strategy\\_en](https://ec.europa.eu/info/publications/sustainable-finance-renewed-strategy_en)

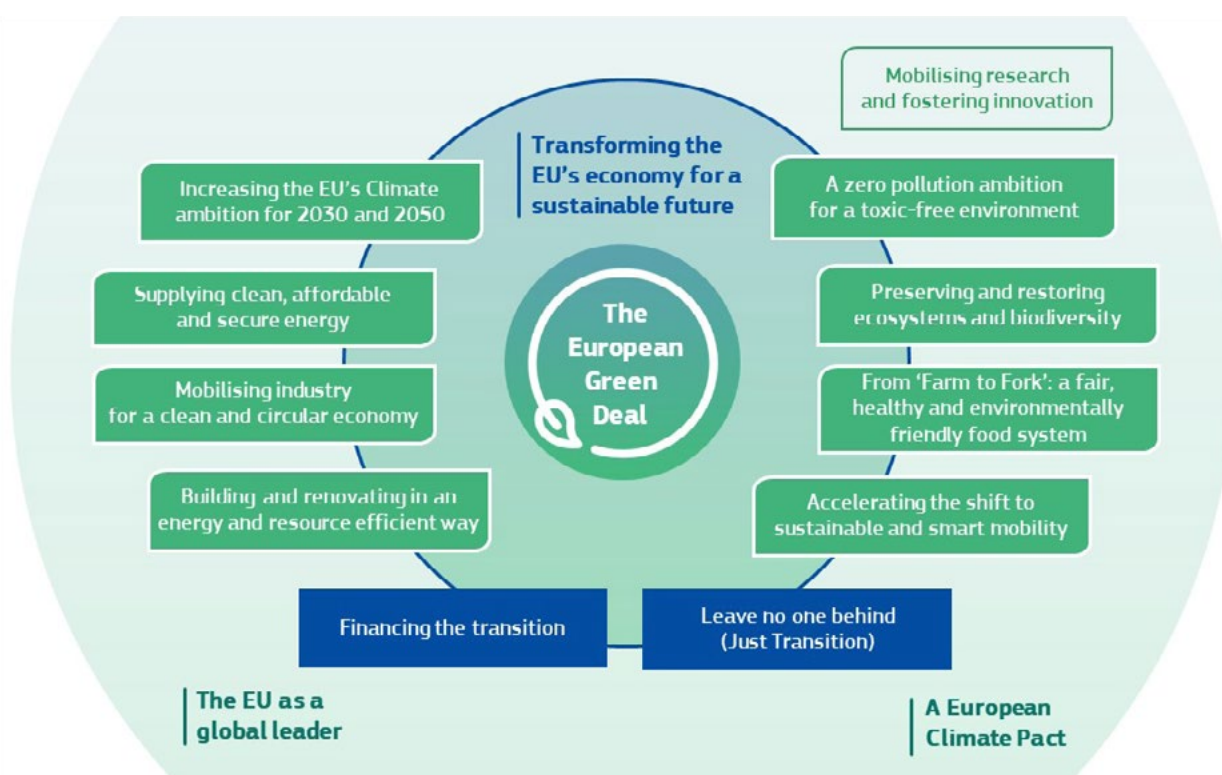
# CREATING A SUSTAINABLE FINANCIAL SYSTEM AND INCENTIVES

The financial sector, as a contributor to climate change and environmental degradation, yet also as a potentially highly significant driver of climate action, has increasingly attracted the attention of EU policymakers. This first manifested through the Action Plan for Sustainable Growth<sup>24</sup> in March 2018 and most recently in the European Green Deal<sup>25</sup> (EGD), published in December 2019.

The Action Plan outlines ten areas of actions to drive more sustainable investment, each of which was translated into a multitude of policies or measures, directed at companies and/or financial institutions, and also at research, Member States and other actors. Policies include, amongst others the EU taxonomy (see table below), creating standards and labels for green financial products and developing sustainability benchmarks. Specifically,

some policies target the risk management of financial institutions, such as incorporating sustainability in prudential requirements.

The EGD clearly outlines finance as a key area that will determine its success, as the mechanism to 'financing the transition'<sup>26</sup>. As part of this, the renewed sustainable finance strategy will lead to further policies and measure to be implemented.



24. [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance_en)

25. <https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1596443911913&uri=CELEX:52019DC0640#document2>

26. European Commission: Communication from the European Commission: The European Green Deal, <https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1576150542719&uri=COM%3A2019%3A640%3AFIN>

# KEY SUSTAINABLE FINANCE POLICIES AND REGULATIONS

Figure 2: Aspects of the European Green Deal; Source: European Green Deal Communication

	Policy/ Regulation	Supervisory Entity	Implementing Agency	Positioning on Sustainable Finance	Year of Implementation	Addresses Climate Change?	Addresses the Safeguarding of Water Resources?	Addresses the Protection of Forests?
1	<b>EU Taxonomy</b>	European Banking Authority (EBA), European Securities and Markets Authority (ESMA), European Insurance and Occupational Pensions Authority (EIOPA)	<p><b>Companies:</b> Corporate Sustainable Reporting Directive (CSRD).</p> <p><b>Fis:</b> Sustainable Finance Disclosure Regulation (SFRD).</p>	<p>Contains six environmental objectives: (1) climate change mitigation; (2) climate change adaptation; (3) sustainable and protection of water and marine resources; (4) transition to a circular economy; (5) pollution prevention and control; and (6) protection and restoration of biodiversity and ecosystems.</p> <p>The EU taxonomy determines economic activities which substantially contribute to at least one of the six environmental objectives, while 'do no significant harm' to any of the other five objectives and following minimum safeguards.</p> <p>With international cooperation and aligned standards being key in shifting financial flows globally, the TEG and the EC have made mentions of potential international alignment of taxonomies.</p> <p>The EU is a co-chair with China of the International Platform on Sustainable Finance (IPSF), working on assessing taxonomies in different countries and developing harmonisation approaches. A first step is the development of a Common Ground Taxonomy as the basis for the establishment of global standards. These discussions are also carried forward by the EU into other international fora, such as the G7 and G20<sup>27</sup>.</p> <p>The final TEG report, published in March 2020, outlines key design principles for globally harmonised taxonomies. The TEG proposes:</p> <ul style="list-style-type: none"> <li>▼ the use of clear environmental goals, such as the 1.5°C temperature goal, to measure performance of economic activities under the respective taxonomy;</li> <li>▼ clear sector and economic activity classifications;</li> <li>▼ metrics to assess environmental performance; and</li> <li>▼ performance thresholds for each economic activity<sup>28</sup>.</li> </ul>	<p><b>July 2020.</b></p> <p>Technical screening criteria for four remaining safeguards expected in 2022.</p> <p>First disclosures using the taxonomy shall be filed in 2022<sup>29</sup>.</p>	<p>The first two environmental objectives turned into technical screening criteria through delegated acts in 2020 are climate mitigation and adaptation.</p>	<p>The taxonomy will address water resources in the third environmental objective.</p>	<p>The taxonomy's criteria to address deforestation as part of climate change mitigation in the first environmental objective have been criticized as being too weak as they classify industrial logging and the burning of trees and crops for energy as 'sustainable' investments.</p>

27. European Commission: Questions and Answers: Taxonomy Climate Delegated Act and Amendments to Delegated Acts on fiduciary duties, investment and insurance advice, [https://ec.europa.eu/commission/presscorner/detail/en/qanda\\_21\\_1805](https://ec.europa.eu/commission/presscorner/detail/en/qanda_21_1805)

28. EU Technical Expert Group on Sustainable Finance (2020): Taxonomy: Final report of the Technical Expert Group on Sustainable Finance, [https://ec.europa.eu/info/sites/default/files/business\\_economy\\_euro/banking\\_and\\_finance/documents/200309-sustainable-finance-teg-final-report-taxonomy\\_en.pdf](https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/200309-sustainable-finance-teg-final-report-taxonomy_en.pdf)

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	Policy/ Regulation	Supervisory Entity	Implementing Agency	Positioning on Sustainable Finance	Year of Implementation	Addresses Climate Change?	Addresses the Safeguarding of Water Resources?	Addresses the Protection of Forests?
2	<b>Corporate Sustainability Reporting Directive (CSRD)</b>	ESMA guidelines for national supervisory authorities	<b>Companies:</b> Companies, including financial market actors, in the EU of a certain size (see scope) will have to start reporting as of 2023	<p>In 2021, the EC put forward a much-anticipated legislative proposal for mandatory reporting<sup>30</sup>. The <b>Corporate Sustainability Reporting Directive (CSRD)</b> proposal amends the Non-Financial Reporting Directive (NFRD) as part of the EU's strategy to strengthen rules on corporate reporting. In 2018, the NFRD introduced requirements for large companies to disclose information on their sustainability risks and impacts. A revision of the directive was announced in 2019 when it was deemed necessary to expand the scope of the companies covered by the requirements and the quality of the information disclosed. The CSRD introduces reporting requirements for a wider range of companies, requiring them to measure their compatibility with 1.5°C scenario analysis, covering more environmental matters and removing the exemption which previously allowed sustainability data to be reported separately<sup>31</sup>.</p> <p>A wider scope of companies is included in the CSRD sustainability reporting obligations:</p> <ul style="list-style-type: none"> <li>as of 2023 all large (500+ employees) and listed companies (including listed SMEs, credit institutions and insurance undertakings, as well as parent PIEs with an average of 500+ employees on a consolidated basis.) will report sustainability information.</li> <li>EU subsidiaries of non-EU companies, as well as any non-EU company with transferable securities listed on an EU regulated market, are also covered by the reporting requirements set out in the CSRD.</li> <li>Climate coverage &amp; TCFD alignment</li> </ul> <p>Although the CSRD references the TCFD in the recitals (§26), it is not explicitly aligned with the standard. Instead, Articles 19a(1) and 29a(1) of Directive 2013/34/EU require undertakings to disclose information on five reporting areas:</p> <ul style="list-style-type: none"> <li>business model;</li> <li>policies (including due diligence processes implemented);</li> <li>the outcome of those policies;</li> <li>risks and risk management; and</li> <li>key performance indicators relevant to the business.</li> </ul> <p>The EC considers the TCFD 'a floor, not a roof' and deems its five reporting areas to be applicable to the reporting needs of European companies.</p> <p>The CSRD introduces the double materiality principle requiring undertakings to report information necessary to understand how sustainability factors affect the undertaking, as well as information necessary to understand the impacts of the undertaking itself on society and the environment. The CSRD introduces detailed reporting requirements which would require companies to report according to mandatory EU sustainability reporting standards, the environmental factors, which include climate change mitigation, climate change adaptation, water and marine resources, resource use and circular economy, pollution, biodiversity and ecosystems. The EU sustainability reporting standards are a linchpin of the EU sustainable finance agenda ensuring consistent reporting rules across the SFDR, the EU Taxonomy and the CSRD, as well as the forthcoming legislation on sustainable corporate governance and due diligence<sup>32</sup>. The standards will be developed by EFRAG with the first set of standards being adopted in October 2022.</p>	<b>Adoption scheduled for 2021, disclosures to start in 2023</b>	Yes, with a reference to 1.5°C goal	Yes, yet will be determined in detail through sustainability standards	Yes, yet will be determined in detail through sustainability standards

29. European Commission: EU taxonomy for sustainable activities. What the EU is doing to create an EU-wide classification system for sustainable activities, [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/eu-taxonomy-sustainable-activities\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/eu-taxonomy-sustainable-activities_en)  
30. European Commission: Corporate sustainability reporting [https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting\\_en](https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en)  
31. CDP: Q&A: Corporate sustainability reporting directive (CSRD) <https://fal.cn/3gejD>  
32. European Commission: Report on development of EU sustainability reporting standards: [https://ec.europa.eu/info/publications/210308-efrag-reports\\_en](https://ec.europa.eu/info/publications/210308-efrag-reports_en)

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	Policy/ Regulation	Supervisory Entity	Implementing Agency	Positioning on Sustainable Finance	Year of Implementation	Addresses Climate Change?	Addresses the Safeguarding of Water Resources?	Addresses the Protection of Forests?
3	<b>Sustainable Finance Disclosure Regulation (SFDR)</b>	ESMA guidelines for national supervisory authorities	<b>Financial institutions</b>	Financial market actor disclosure requirements: The <b>SFDR</b> , set to roll out in several stages over the next two years, contains reporting obligations at both the company and product level, and entails a comply-or-explain assessment of the main negative impacts their investments will have on the environment and society. The SFDR provides a scope for financial market participants to integrate sustainability risks, to systematically consider and integrate sustainability risk in a consistent way in their investment decisions and for disclosure aspects. The aim is to enhance comparability of financial products and reduce greenwashing. The Regulation came into force end of December 2019 and applies from March 2021 <sup>33</sup> .	<b>Came into force in March 2021.</b>	Yes, it interrelates with the environmental objectives of the taxonomy.	Yes, it interrelates with the environmental objectives of the taxonomy.	Yes, it interrelates with the environmental objectives of the taxonomy.
4	<b>Sustainable Corporate Governance</b>	Currently national competent authorities at Member State level	<b>Companies</b>	Sustainable sourcing and supply chain transparency are increasingly being recognized not only as an important part of a company's environmental strategy, but also as a fundamental part of a sound overall business strategy. As outlined in the EGD, the EC has put forward an initiative on <u>sustainable corporate governance</u> . The adoption of the initiative by the EC is expected for autumn 2021. The European Commission looks at aspects such as directors' duty of care, due diligence duty and stakeholder engagement as well as expected impacts of possible measures, such as related costs, <b>improvement</b> in risk management and resilience and the environmental performance.	<b>2021-2026</b>	Yes, as part of the risk assessment and environmental performance.	Yes, as part of the risk assessment and environmental performance.	Yes, as part of the risk assessment and environmental performance.
5	<b>EU legal framework to halt and reverse EU-driven global deforestation</b>	Foreseen: national competent authorities at Member State level.	<b>Companies</b>	Upon a resolution from the EP, the EC is now required to present an EU legal framework to halt and reverse EU-driven global deforestation by autumn 2021. The proposal is to require all Forest Risk Commodities (FRCs) placed on the EU market to be produced in accordance with sustainable production, deforestation-free criteria, and protecting indigenous communities' human rights. This resolution for a new EU legal framework calls for mandatory due diligence, corporate reporting, disclosure, and third-party participation requirements. By introducing due diligence legislation on FRCs, the EU could speed up business transitions to deforestation-free supply chains.	<b>Proposal by the EC expected for autumn 2021.</b> The legislative file's timeline was pushed back amidst pressure from business <sup>34</sup> .	Yes, as halting deforestation is a key aspect of climate mitigation.	Water resources are not part of this legislative proposal.	Yes, deforestation risk commodities in companies' supply chains are the focus area of this legislative proposal.

Nb: This is not an exhaustive list of actors but key regulatory and policy initiatives in the EU

33. European Commission: Sustainability-related disclosure in the financial services sector. What the obligations are for manufacturers of financial products and financial advisers towards end-investors, [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/sustainability-related-disclosure-financial-services-sector\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/sustainability-related-disclosure-financial-services-sector_en)

34. Aarup, S. A., Moens, B., Leali, G. and von der Burchhard, H. (2021): Europe Inc. wins as EU delays new business rules, Politico, 21/05/2021, <https://www.politico.eu/article/europe-inc-puts-brussels-new-business-rules-on-ice/> [Accessed on 08/08/2021]



# ANALYSIS (INCLUDING GOVERNANCE CHALLENGES) AND WAY FORWARD

## Key EU governance challenges

The large number of actors involved in the policy process often leads to lengthy legislative decision-making processes. In contrast, the pace of the legislative implementation of the sustainable finance legislative has been significant (also in comparison to other climate legislation).

Generally, the adoption of climate policies and measures has picked up in speed over the last year, with sustainable finance as a clear priority. While these are encouraging developments for climate and environmental action in the EU, it reduces acceptance by some actors<sup>35</sup>.

## Outlook on the CSRD

The CSRD is a very advanced mandatory reporting framework in international comparison, covering a large number of companies including financial market actors in the EU. The CSRD represents a big step towards more detailed corporate reporting requirements, yet implementation and enforcement are critical for its success. While the technical criteria of the reporting requirements are due to be defined by EFRAG, some technical details should be included in the level 1 text of the CSRD law. Although the CSRD references the need for companies to adhere to 1.5°C trajectory, there is currently no mention of science-based targets. The reference to 1.5°C in the CSRD shows that the EC is reflecting science, yet this aspect needs to be strengthened further. Including a reference to the latest climate science and the IPCC in the CSRD text would ensure that the reporting requirements keep pace with any relevant and necessary development in the science. The ability of companies to

implement their 1.5°C plans requires public and private investment in sustainable business, research and innovation. Currently, there is a unique opportunity to match private investment with public funds, by utilizing the recovery funds and member states budgets for critical finance to the transformation of the EU economy.

While the CSRD references the need for value chain emission reporting, it does not specifically focus on the importance of scope 3 emissions. This is crucial especially for emission reduction target setting of companies. Additionally, the CSRD needs stronger wording on water security and commodity-driven deforestation. Finally, the CSRD proposal only requires limited assurance, but inclusion of both reasonable assurance and external verifications on reported data for GHG emissions could result in a higher level of assurance than limited and moderate assurances.

## Outlook on the taxonomy

Amendments to the taxonomy regulation, as stipulated in the legislative text, can be made by the EC through delegated acts, meaning they don't have to go through the full legislative process. The delegated acts for the technical screening criteria for climate mitigation and adaptation were proposed in November 2020, leading to harsh criticism by a wide range of stakeholders. Opinions differed significantly on the classifications made on nuclear power, natural gas and biomass. At this stage, nuclear power and natural gas are

neither included nor excluded from the classification. The agriculture sector has been removed from delegated acts and will be taken up at a later stage in connection with biodiversity aspects. Environmental groups criticized the treatment of natural gas, forestry and biomass in particular, stating the use of these energy sources are not in line with Paris-aligned emission reduction scenarios. Following this controversy, environmental groups temporarily suspended their memberships of the EU Platform on Sustainable Finance<sup>36</sup>.

35. Harvey, F. and Rankin, J. (2020): What is the European Green Deal and will it really cost €1tn?, The Guardian, 09 March 2020, <https://www.theguardian.com/world/2020/mar/09/what-is-the-european-green-deal-and-will-it-really-cost-1tn> [Accessed on 07/08/2021]

36. Simon, F (2021): NGOs walk out on EU green finance group over forestry, bioenergy rules, EURACTIV, 22. Apr. 2021 (updated: 27. Apr. 2021), <https://www.euractiv.com/section/energy-environment/news/ngos-walk-out-on-eu-green-finance-group-over-forestry-bioenergy-rules/>; Open letter 'Letter to the Commission on EU taxonomy Climate DA March 2021', [https://wwf.eu.awsassets.panda.org/downloads/letter\\_to\\_european\\_commission\\_on\\_eu\\_taxonomy\\_delegated\\_act\\_march\\_2021.pdf?utm\\_source=Press+List+WWF+EPO&utm\\_campaign=9c06e28702-EMAIL\\_CAMPAIGN\\_2020\\_09\\_08\\_11\\_27\\_COPY\\_01&utm\\_medium=email&utm\\_term=0\\_12dfb21e9b-9c06e28702-413385781](https://wwf.eu.awsassets.panda.org/downloads/letter_to_european_commission_on_eu_taxonomy_delegated_act_march_2021.pdf?utm_source=Press+List+WWF+EPO&utm_campaign=9c06e28702-EMAIL_CAMPAIGN_2020_09_08_11_27_COPY_01&utm_medium=email&utm_term=0_12dfb21e9b-9c06e28702-413385781)

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By endorsing the CDP disclosure system, governments can actively drive the increase in quantity and quality of climate and environmental data of corporates and local governments as well as action on climate change, water insecurity and deforestation.

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