Recommendations of the Scientific and Expert Committee on key sectoral indicators for sustainable finance

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Policy Statement

The Scientific and Expert Committee (SEC) notes that the actions of the Sustainable Finance Observatory ("*Observatoire de la Finance Durable*") will be all the more useful if they respect five major principles which are found in many of our recommendations:

- **Transparency**
- **Readability**
- **Coherence**
- **Reliability**
- **Relevance**

These five main principles should be the pillars of each indicator published in the Sustainable Finance Observatory.

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Point of attention

Given the time taken to work on and publish the recommendations in this document, some of them have been partially implemented on the Sustainable Finance Observatory website following its annual update on 28 October 2022.

The SEC has identified changes to the site that impact the formulation of the following recommendations:

- Cross-cutting proposals, Section 3, Recommendation 3: The scope covered by each indicator is no longer specified at the top of each section, but on a separate page (Calculation methods). The SEC notes that the information on the representativeness and origin of the data presented has been improved, and welcomes the Observatory's work on this matter. Nevertheless, the SEC maintains its two recommendations (3.1 and 3.2): it remains necessary to publish, for each federation, the overall representativeness of the data through the requested indicators; in addition, the use of extrapolations should be kept to a minimum, and duly justified where appropriate.
- Proposals for the theme "ESG practices and products": The themes "responsible management" and "responsible product offering", present in the previous version of the Observatory website, have now been merged into a single theme called "ESG". The SEC appreciates this move, which is in line with the spirit of recommendation 1 of this sub-section of the report. Nevertheless, it maintains its recommendation to ensure that this change will be maintained in future updates of the site, and also suggests that the following name be adopted for this section, which it considers more accurate: "ESG practices and products".

Translate by Simon Messenger. French version is the original one.

I. Executive summary

In order to present the data from the federations in a more accurate, structured and harmonised way, the Scientific and Expert Committee (SEC) carried out an evaluation of the current publication process. It identified several shortcomings: lack of harmonisation between the different themes; lack of accuracy regarding the coverage and scope of the indicators; absence of data from certain federations as well as missing historical data...

In order to address these weaknesses, the SEC has issued a list of recommendations to be implemented in the short term (i.e. at the time of the 2023 publication relating to the 2022 financial year) when they involve "minor" changes to the presentation of information; or in the medium term (i.e. at the time of the 2024 publication relating to the 2023 financial year) when they involve more profound changes to the data collected and published.

1. The first set of recommendations is cross-cutting

[Recommendations to be implemented in the short term]

1.1. Harmonise the reporting structure within the different themes and the key performance indicators (KPIs) presented therein;

1.2. Systematically specify, for each published indicator, the amount and proportion of the associated business volume (in €bn and % of the total associated business volume, respectively);

1.3. Systematically specify, for each indicator, the representativeness of the volume of activity published in relation to the total volume of activity of each federation; in addition, refrain from using extrapolations aimed at broadening the scope of the data presented;

1.4. Increase the volume of historically published data;

1.5. Harmonise the annual questionnaire sent to the federations with the publication structure recommended by the SEC;

[Recommendations to be implemented in the medium term]

1.6. Ensure an exhaustive publication from all federations and, failing that and as a transitional measure until 2023, adopt a "comply or explain" approach by specifying the deadline for publishing the missing data;

1.7. Extend the scope of partner federations to other business lines by entering into discussions with ASPIM and AMAFI.

2. **The second set of recommendations concerns ESG (Environmental, Social and Governance) issues**

[Recommendations to be implemented in the short term]

2.1. Improve the readability of the "responsible management" and "responsible product offering" themes by merging them;

2.2. Adopt a simplified and readable reporting structure common to all federations;

2.3. Adjust and complete, through minor modifications, some published indicators:

2.3.1. Adjust the indicator on exclusion policies, in particular by specifying the activity metric used and by indicating the cases of non-application found;

2.3.2. Clarify the contextual information accompanying the indicator on labelled funds and harmonise the geographical scope of the labels mentioned;

2.3.3. Delete the indicator on membership of international coalitions and initiatives;

[Recommendations to be implemented in the medium term]

2.4. Publish new indicators and adjust existing ones to better reflect the transformation of financial practices and flows:

2.4.1. Publish a new indicator on the average share of remuneration indexed on ESG criteria;

2.4.2. Publish a new indicator on engagement or dialogue processes related to ESG issues;

2.4.3. Publish a new indicator reflecting which of the entities engaged in an engagement or dialogue process have met the demands of financial institutions or have been subject to an escalation process;

2.4.4. Publish a new indicator on the tabling of resolutions, the support of resolutions or the inclusion of resolutions (on the agenda of the board of directors or supervisory board) in favour of ESG issues;

2.4.5. Replace the indicator on shareholder engagement with a specific indicator on the distribution of votes on ESG-friendly resolutions; in addition, extend this indicator to the banking business lines;

2.4.6. Complete the contextual information accompanying the indicator on activities falling under category 1 of the AMF classification; in addition, extend its publication to all federations;

2.4.7. Clarify the indicator on "Article 8 and 9" products of the SFDR Regulation, in particular by disclosing the share of activity aligned with the green taxonomy; also extend its publication to entities affiliated to France Invest (FI) and the French Banking Federation (FBF);

2.4.8. Clarify the indicator on sustainable bonds, in particular by mentioning the standards upon which they are based; also propose a new indicator, parallel to this one and specific to the FBF, on loans granted promoting sustainability characteristics;

2.4.9. Complete the indicator on financial inclusion, notably by specifying the concepts to which it refers; also extend this indicator to entities affiliated to France Assureurs (FA) and the Association des Sociétés Financières (ASF).

In general, the SEC recommends that publications be as comprehensive as possible.

3. **Finally, the third set of recommendations concerns the transition to a carbon neutral economy**

[Recommendations to be implemented in the short term]

3.1. Improving the introductory sections of the "Transition to a carbon neutral economy" theme
3.2. Communicate the share of actors with carbon neutrality transition objectives
3.3. Publish indicators on the alignment measurement tools used by stakeholders
3.4. Categorise actors according to the nature of the instruments used to assess climate risks
3.5. Communicate indicators on the environmental impact of financial actors
3.6. Publish funding amounts in line with the European taxonomy
3.7. Show the share of investment and financing related to the highest emitting sectors (including that benefiting companies engaged in the transition), and the net proceeds associated with service activities carried out for the benefit of the highest emitting sectors

3.8. Display the share of investments and financing linked to companies committed to a credible transition

[Recommendation to be implemented in the medium term]

3.9. Develop an aggregate sectoral measure of portfolio alignment (finance and investment)

Finally, the SEC highlights some weaknesses regarding disclosures on hydrocarbons - coal on the one hand and oil and gas on the other hand. Indeed, data on fossil fuels are regularly incomplete, including on the exposure of market players (in flows and stocks).

As such, a number of ideas are put forward which will be the subject of a future dedicated publication.

II. General introduction

- Since the July 2019 Market Declaration[1] , the efforts of the main member federations of the Observatoire de la Finance Durable (OFD) have aimed to highlight the transformation of the financial sector towards a sustainable growth model. This effort to raise visibility has resulted, in particular, in the annual publication of sectoral data on the transformation of financial practices and flows.
- The SEC, whose mandate is to ensure the scientific rigour of the Observatory, decided to assess the relevance and readability of the sectoral information published. At the end of this review, it notes the efforts made within the Observatory in terms of sectoral information and the regular increase in the information published by the federations.
- It notes, however, that the sectoral indicators presented still need to be improved, as they are often characterised by :
    - significant heterogeneity, rarely justified by the diversity of sectors (banking, insurance, portfolio management, etc.),
    - the inadequacy of the distinction between "activities" of companies and "companies" as a whole,
    - the lack of a reference or benchmark against which to judge the significance of the indicators, and
    - incomplete coverage of the perimeter to give an overall view of the transformation of the financial sector activities.
- The climate emergency and the current energy situation, particularly as a result of the war in Ukraine, remind us of the need for more in-depth and precise monitoring of financial support for the transition and for fossil fuels. The SEC's recommendations on sectoral indicators are therefore aimed at improving the market's tools in order to be able to monitor all these developments as effectively as possible. "We can only pilot well what we measure well". In particular, distinctions were made between short-term and medium-term indicators where relevant, as well as between means-based indicators and results-based indicators.
- In any case, it is neither desirable to aggregate or to compare indicators between different federations, given the specificities of each federation's activities requiring appropriate indicators. Additionally, there is a risk of double counting.
- The SEC proposes a series of recommendations, organised by theme: 1. cross-cutting recommendations; 2. recommendations on ESG products and practices; and 3. recommendations on the transition to carbon neutrality. In addition, the SEC publishes a statement of intent on its future work on hydrocarbons

[1] "Déclaration de Place: a new step for green and sustainable finance", https://financefortomorrow.com/actualites/declaration-de-place-financiere-une-nouvelle-etape-pour-une-finance-verte-et-durable/

III. Cross-cutting proposals

a. Introduction

The SEC notes that a large quantity of sectoral data is published on the OFD website. The multiplication of the information published, as well as the lack of harmonisation in the structure and typology of the headings and indicators presented, are likely to generate "noise", which can be a source of confusion and incomprehension on the part of the reader - whether or not the latter is a user of the information. This "white noise"[2] generated by the quantity of data currently listed may also lead to the publication of information that has no added value (in terms of the Observatory's stated objective of transformation) to the detriment of the publication of more relevant indicators.

Consequently, it is necessary to review the published indicators and to simplify and reorganise the themes and headings presented. In this context, the SEC wished to formulate recommendations in two areas: the first relates to the presentation of information and aims in particular to harmonise and clarify the data published; the second aims for a more exhaustive disclosure of information as well as an extension of the OFD's scope of coverage. Each recommendation is accompanied by a time scale for its application: short or medium term. The recommendations on the presentation of information, in the short term, are to be implemented by the next publication (i.e., the 2023 reporting on the 2022 financial year); the recommendations on the completeness and extension of publications, in the medium term, are to be implemented by the 2024 reporting on the 2023 financial year, and, at the latest, the 2025 reporting on the 2024 financial year.

In any case, the SEC reiterates that it is currently not desirable to aggregate or compare indicators between different federations, given the specificities of each federation's activities, which require appropriate indicators. In addition, there is a risk of double counting.

b. Recommendations

- **<u>Section 1: Harmonising the reporting structure and type of indicators presented</u>**

<u>Finding:</u>

The headings of each theme suffer from a lack of harmonisation in terms of their titles and the type of key performance indicator (KPI) presented. Some information is present for some actors but absent for others, without this being justified by the nature of the activity specific to each "business" or sector[3].

[2] Frank Elderson - Keynote speech: "Full disclosure: coming to grips with an inconvenient truth" (March 2022)

[3] These differences can be seen in the following headings: "Extra-financial integration in traditional analysis", "Extra-financial dimension in engagement", etc.

Goal of the SEC:

To improve the readability of information published by the federations.

Recommendation #1 *[short term]* :

Harmonise the reporting structure and the KPIs presented in each theme, in particular by removing certain headings/sub-headings within each theme (cf. recommendation #2 of the specific section "responsible management/products").

- **Section 2: Specify the amount and proportion of business volume associated with the published indicators**

Finding:

The indicators currently published incorporate separate coverage parameters (stocks, products, entities, transactions, etc.).

Goal of the SEC:

To improve the understanding of the real dynamics taking place in each federation and to better understand the perimeters covered by the indicators.

Recommendation #2 *[short term]* :

In this context, and for each quantitative indicator, the SEC **again recommends**[4] to systematically publish the amount and percentage of the total volume of activity, in €bn and % of total activity, respectively.

The choice of the relevant metric will be made according to the relevant activity, in particular on the basis of the typology of financial activities listed respectively in Annexes III-IV (asset managers), V-VI (credit institutions), VII-VIII (investment firms), IX-X (insurance and reinsurance undertakings) of the Delegated Regulation 2021/2178 of the European Commission of 6 July 2021[5] .

[4] This recommendation has been made by the SEC in previous publications (2021).

[5] Commission Delegated Regulation 2021/2178 of 6 July 2021 supplementing Regulation (EU) 2020/852 of the European Parliament and of the Council with details of the content and format of the information to be published by undertakings subject to Article 19a or Article 29a of Directive 2013/34/EU on their environmentally sustainable economic activities, and the method of complying with this information requirement

- **<u>Section 3: Clarifying the scope of published indicators</u>**

<u>Finding:</u>

For each of the partner federations, the indicators currently reported cover data from all or part of their entities. The scope covered is currently mentioned at the beginning of each section[6] . In this respect, the SEC welcomes the publication efforts made by France Assureurs to provide a clear and understandable scope as to the entities covered by each indicator.

However, the SEC notes that this practice is not harmonised for all federations. In particular, some federations do not explicitly mention the number of respondents and their proportion in relation to the total number of entities affiliated to the federation. Similarly, the volume of activity associated with the respondent entities, as well as its proportion in relation to the total volume of activity of each federation, are not systematically published.

Finally, in some cases, the use of extrapolations may bias the quality and interpretation of published data. In particular, the SEC is concerned that extrapolations may compensate for the lack of reporting from entities with poor performance (or, *at the very least*, weaker performance than the average for the federation) with regard to environmental, social and governance issues, and thus artificially improve the published results.

<u>Recommendation #3.1 *[short term]* :</u>

The SEC insists on the need to clearly indicate the representativeness of the data published on the OFD website.

In this context, in order to bring more precision to the published data, the SEC recommends that the following information be explicitly indicated at the beginning of each theme for each federation:

- The ratio between (1) the amounts covered by the "responding" entities that provided the data associated with the indicator and (2) the total amounts covered by all entities affiliated to the federation.

For example : $\frac{\textbf{\textit{total amount of bonds held by responding entities}}}{\textbf{\textit{total amount of bonds held by all entities affiliated to the federation}}}$

- The number (in absolute terms) and proportion (as a percentage of the total) of entities that provided data for the indicator.

Finally, for any indicator that is not subject to the same scope of coverage as that indicated at the beginning of each theme, it appears necessary to specify the information mentioned above for the relevant indicator.

[6] By way of introduction (blue font)

For example, the statement expected for the AFG would take the following form: "Data from [x] entities (i.e. [x]% of the federation's members) representing [x]% of the total assets under management by AFG-affiliated entities.

Recommendation #3.2 *[short term]* :

The SEC recommends that extrapolated data should not be used, but rather that real information should be published.

This recommendation specifically addresses the case where actual data from a subset of a given population is extrapolated to the whole population.

- **Section 4: Amplifying historically reported data to assess changes in the performance of financial actors**

Finding:

Some of the indicators currently published do not (or unevenly) incorporate sufficient historical background[7] to allow an analysis of the evolution of the transformation of financial sector practices.

Recommendation #4 *[short term]* :

The SEC recommends that federations publish their data over as long a period as possible, and *at least* over an interval of three successive years (N-1, N-2 and N-3, with N being the year of publication in progress) in order to observe a trend and note any changes in practices and flows.

More specifically, the SEC considers it essential that the federations publish, for historical purposes, all the data requested for the years 2020 and 2021 and, ideally, for 2019.

- **Section 5: Harmonising the annual questionnaire with the recommendations of the SEC on the organisation of the structure and indicators[8]**

Finding:

The annual questionnaire sent to the federations contributes to the structuring of the reporting exercise proposed by the OFD to financial institutions. In this context, the SEC believes that the

[7] For some indicators, only one year is published; for others, three years are published.

[8] This recommendation is also addressed to the OFD

questionnaire should reflect the structure proposed in its recommendations, in a spirit of consistency and in order to best promote these recommendations.

Recommendation #5 *[short term]* :

The SEC recommends that the annual questionnaire sent to the federations be harmonised with the reporting structure recommended by the SEC in its recommendations.

- **Section 6: Ensure comprehensive publication by all OFD partner federations**

Finding:

The SEC notes the recurring absence of data from several federations on the majority of the themes and indicators presented. This absence is all the more unjustified since the partner federations committed themselves, at the time of the creation of the OFD, to publishing their data[9] .

Therefore, the SEC proposes a two-step approach to overcome this lack of information.

Recommendation #6 *[medium term]* :

1. Justify the lack of publication of information and determine an associated publication schedule by applying, on a temporary basis, the "comply or explain" approach . In addition, the federations should systematically indicate the date on which the data will be published, without this date exceeding 2 years after the last publication of information *(e.g. in the case of missing data in the 2022 publication relating to the 2021 financial year, this should be published at the latest in the 2023 publication exercise relating to the year 2022).*

2. Publish the missing data for the years 2020 and 2021, with a view to ceasing all use of "comply or explain" from 2024 (for the reference year 2023).

- **Section 7: Extending the scope of partner federations to other trades**[10]

Finding:

[9] See OFD: *"Banks, insurers, management companies, private equity and other credit finance companies have committed, via their professional federations, to publish their data to testify to their transformation towards sustainable finance by giving reading indicators particularly oriented towards the climate and alignment with the objectives of the Paris Agreement."*

[10] This recommendation is addressed primarily to the OFD.

The OFD centralises data from several federations representing the financial sector in France. However, several federations are not yet partners of the Observatory and could provide relevant information in addition to that currently published on the Observatory's website.

Recommendation #7.1 *[short term]* :

The SEC again recommends broadening the base of partner federations by including the business lines relating to the management of unlisted real estate funds, represented by the Association Française des Sociétés de Placement Immobilier (ASPIM).

Recommendation #7.2 *[medium term]* :

Similarly, the SEC recommends that the OFD initiate discussions with the French Financial Markets Association (AMAFI)[11] in order to consider its integration into the OFD's partner federations. This recommendation is made in view of the leading role played by the AMAFI in representing financial market participants and activities (indices and exchanges, market infrastructure and post-trade operators, derivatives, investment firms).

[Conclusion]

The need to ensure overall consistency in the structure of the reporting of information on the OFD website

Finding:

The current structure of the OFD reporting, divided into four themes and divided by federation, can be explained by the historical preponderance of certain subjects - including the exclusion of the coal sector, for example - at the heart of the issues relating to the development of sustainable finance. Nevertheless, it does not appear to be very well suited to enabling the various stakeholders (from financial actors to site readers) to achieve overall consistency in the way financial institutions take into account environmental, social and governance issues. There are several reasons for this:

- The different themes and sub-themes are not exclusive by design and in fact present redundant aspects[12] , making it more difficult to find specific indicators in the report;
- The articulation of the different sub-themes does not necessarily follow a logical order: coal-related policies and strategies could belong to the theme "transition to a carbon-neutral

11 See AMAFI's institutional website

12 It is worth noting, for example, that from the perspective of management companies, the current themes of "Exit from Coal" and "Responsible Management" both address the issue of exclusion - exit from coal being in fact only one exclusionary practice in particular.

economy"; "responsible management" could group together the themes of "transition" and "responsible products", etc. ;

- The current structure endorses the differentiated reporting of information by each of the federations, which is the subject of a request for harmonisation by the SEC, upstream (questionnaire) and downstream (published data), cf. recommendations #1 and #8, respectively.

In this context, it would seem appropriate for the OFD, the federations and the SEC to reflect on the gradual adoption of a new reporting structure, in particular to guarantee the overall coherence and articulation of the themes listed. In particular, it seems necessary that the different themes be complementary and mutually exclusive and cover the different ESG aspects, and that the division by federation - sometimes too personalised - give way to a harmonised structure.

On a practical note, a proposal for an alternative structure to the present one could be the subject of future work by the SEC and presented at the next iteration.

IV. Proposals for the themes "Responsible Management" and "Responsible Products

a. Introduction

The recommendations on indicators (KPIs) in this section are intended to suggest a common baseline for each indicator for all federations. Within this framework, the SEC recommends a series of indicators based on common subjects and issues, but with different applications, particularly according to the specific characteristics of each profession.

In this respect, the SEC may propose, for the same indicator: (1) different terminologies, (2) a "focus" on a specific activity (banking, insurance, etc.), and/or (3) an exemption for all or part of the relevant business line.

This common base of differentiated application has been defined in order to allow coherence and better readability for the non-initiated reader, while allowing each federation to faithfully reflect the reality of its members' activities.

Therefore, the SEC does not recommend a single indicator for all federations. Each federation should adapt its publication according to the trade.

In any case, it is not advisable to aggregate the indicators between different trades given the specific nature of the activities of each of them, which require appropriate indicators. Similarly, aggregating and/or comparing data from different federations does not appear to be relevant, particularly because of the risk of double counting.

b. Recommendations

Executive summary

The themes of "responsible management" and "responsible product offering" are intended to reflect, in an aggregated manner, the practices implemented across the entity and those at the level of the financial products and services managed. In addition, the federations present key performance indicators that should make it possible to measure the transformation of the practices and financial flows of financial players, with the aim of making a positive contribution to achieving ESG objectives.

In this respect, it is essential that the information published reflects the transformation of the flows and practices of financial players. Otherwise, the analysis and understanding - by the financial institutions themselves as well as by their stakeholders (clients, regulators) - of the impact of the strategies implemented and the products and services they market could be made difficult or even biased. As a result, the lack of clarity and completeness of published information may lead to ill-informed decisions and hinder the achievement of broadly stated environmental and social objectives.

These decisions are also likely to have a significant impact on the reputation of financial institutions and the trust placed in them by their stakeholders.

After analysis, the SEC notes that the information currently published does not sufficiently reflect the transformation of the flows and practices of financial institutions and must be substantially improved, both in terms of form (presentation and structure of the information) and substance (comparison and "transformative" scope of the indicators published).

The SEC's recommendations for this section are organised around two dimensions: the first relates to aspects of presentation of information and may apply to the reporting to be made in 2023 on the financial year 2022. The second relates to the need to review the published indicators and associated data, notably *through* the inclusion of new indicators, the replacement and/or deletion of existing indicators. In this context, on the one hand, the SEC recommends restructuring the information published in order to make it easier to read and understand. In particular, the current themes of "responsible management" and "responsible product offering" should be merged into a single category ("Environmental, social and governance (ESG) practices and products"), and the publications of the various federations should be standardised into a common structure. The proposed reorganisation guarantees better readability and simplified access to information. On the other hand, the SEC recommends that the KPIs be overhauled, ensuring that they reflect the degree of transformation of financial practices as closely as possible, and that they are precisely defined and leave as little room for interpretation as possible. As such, new indicators on engagement and dialogue and on remuneration are proposed; clarifications are made on the indicators "labels", "bonds/loans", "AMF", "SFDR" and "financial inclusion"; and the proposal to eliminate the indicator on membership of initiatives is made. At the same time, the SEC stressed the importance of the most comprehensive publication possible by all the relevant federations.

Finally, and in the interests of overall consistency of the document, the SEC recommends that the cross-cutting recommendations set out in the previous section be systematically applied to each of the recommendations in this section, namely: harmonisation of the publication structure used; systematic announcement of the representativeness of the data published; display of the historical data over a minimum period of three consecutive years; justification for the absence of publication of information (particularly on the part of "partner" federations); extension of the scope of the OFD exercise to the ASPIM; harmonisation of the annual questionnaires, etc.

The chart below summarises the main recommendations and the recommended structuring of the "ESG practices and products" section. The 11 suggested indicators are divided into two sub-themes ("Entity practices and strategies" and "Products and services"). The SEC also identified 6 indicators as "priority" indicators (in green in the table below) by virtue of their transformative aspect of the activities of OFD member federations. However, the SEC considers that the communication of these "main" indicators does not exempt the publication of the other indicators, which can nevertheless provide a complementary vision of the federations' commitment to ESG objectives.

Section #1 : une thématique unique

Section #2 : une structure simplifiée, commune à toutes les fédérations

Section #3 : une liste d'indicateurs-clés de performance

Section #4 : une publication exhaustive de la part de chaque métier/fédération

Pratiques et produits environnementaux, sociaux et de gouvernance

<table>
<tr><th>Sous-thématique #1</th><th>pratiques et stratégies "entité "</th><th>AFG</th><th>FA</th><th>FBF</th><th>FI</th><th>ASF</th></tr>
<tr><td>ICP 1</td><td>Politique d'exclusions</td><td colspan="5">X</td></tr>
<tr><td>ICP 2</td><td>Rémunération</td><td colspan="5">X</td></tr>
<tr><td>ICP 3</td><td>Engagement / Dialogue</td><td colspan="4">X</td><td>X</td></tr>
<tr><td>ICP 4</td><td>Processus d'escalade</td><td>X</td><td>X</td><td>X</td><td>X</td><td>X</td></tr>
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<tr><th>Sous-thématique #2</th><th>"produits et services"</th><th>AFG</th><th>FA</th><th>FBF</th><th>FI</th><th>ASF</th></tr>
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<tr><td>ICP 8</td><td>Règlement SFDR (art. 8 et art. 9)</td><td>X</td><td>X</td><td>X</td><td>X</td><td>X</td></tr>
<tr><td>ICP 9</td><td>Fonds labellisés</td><td colspan="4">X</td><td>X</td></tr>
<tr><td>ICP 10</td><td>Obligations et prêts</td><td colspan="5">X</td></tr>
<tr><td>ICP 11</td><td>Inclusion financière</td><td>N/A</td><td>X</td><td>X</td><td>N/A</td><td>X</td></tr>
</table>

En vert : KPIs à publier en priorité

X	*Recommended publication*
X	*Recommended publication with possible trade exemptions (to be justified)*

Part I: Cross-cutting recommendations on the structure of the publication

Section #1 *[short term]*: a need for greater clarity between the existing themes of "responsible management" and "responsible product offering"

Finding:

The existing[13] themes "Responsible Management" and "Responsible Product Offering" share common indicators (sector policies, integration of environmental, social and governance (ESG) aspects) that may call into question the relevance of two separate categories; similarly, the same indicator is published under a different theme depending on the relevant federation[14] . Finally, some information published under the "responsible products" theme is not specific to this theme and could be published under the "responsible management" theme[15] . In this context, it seems that the existence of two themes

[13] Or "themes".

[14] See information on sectoral policies

[15] Heading "Offer products covered by a sectoral policy" (data published in terms of management company share and total assets)

is not justified; this situation may lead to confusion and misunderstanding on the part of an uninformed reader wishing to quickly access the information sought.

Objective of the ESC :

Simplify and improve readability for all stakeholders.

Recommendation #1:

The SEC recommends merging the themes "Responsible Management" and "Responsible Products" into a single category called "Environmental, Social and Governance (ESG) Practices and Products".

Section #2 *[short term]*: Adopt a simplified and readable reporting structure common to all federations

Finding:

The merging of the themes mentioned above should make it possible to simplify and clarify the structure within which the data will be published, in order to facilitate access to and understanding of the data. In fact, the current publication shows about ten distinct subcategories/headings[16] .

Indeed, the multiplication of categories/subcategories/headings as well as the surplus of information inherent in the existing structure can be detrimental to the access, comprehension and readability of the published data, *a fortiori* for an uninformed public.

Recommendation #2:

The SEC recommends structuring the disclosures by adopting a simplified and readable approach, **divided into two sub-themes, within the theme "Environmental, social and governance practices and products"** in financial practices and products"**:** the first sub-theme would reflect the practices and strategies implemented at the entity level; the second sub-theme would reflect the observed practices relating to financial products.

To this end, the SEC recommends **avoiding the addition of an "intermediate" or supplementary heading**. Within the theme "Integration and management of environmental, social and governance aspects in financial products and practices", the following structure should appear:

(1) Sub-theme #1 ("entity") ;

[16] Products integrating environmental or social objectives; extra-financial offer in products; sectoral policy; responsible investment practices; shareholder engagement; participation in initiatives / coalitions; financial inclusion; sustainable investment practices; responsible investment practices; labelled funds...

(1.1) Key Performance Indicator #1 ;

(1.2) Key performance indicator #X ;

(2) Sub-theme #2 ('products') :

(2.1) Key Performance Indicator #1 ;

(2.2) Key Performance Indicator #X

A structure is proposed in recommendation #4 of this section.

Finally, the SEC recommends that the published indicators be numbered in line with the **numbering proposed in recommendation #3 in this section**.

Part II: Specific recommendations on key performance indicators

This section focuses on proposals to complement, replace or remove existing KPIs, as well as the creation of new KPIs - whether or not inspired by existing ones. These proposals should meet the primary objective of the OFD: to inform the transformation of five businesses: insurance, banking, private equity, asset management, and other financial services.

At the same time, the SEC is urging the federations to consider the cross-cutting recommendations mentioned earlier in this report.

Section #3: publishing indicators that reflect the transformation of financial practices and flows[17]

- *Sub-theme #1: "Entity-wide practices and strategies*

Sectoral exclusion policies

Finding:

An indicator related to "sectoral policies" is currently published by three federations (AFG, FA and FBF), but in its current form seems to suffer from the absence of a "transformative" component aligned with the objectives governing the publication of OFD data: the transformation of practices and the redirection of financial flows.

Indeed, the existence of an ESG policy directed towards exclusions, if it is neither robust – i.e. based on science- nor credible – i.e. accompanied by a high level of involvement of governance bodies, and an active and recurrent engagement with the relevant sectors - does not lead to the transformation

[17] These indicators are not ranked in order of importance

towards sustainable practices. For instance, recent work indicates that exclusionary investment policies should not be considered as sustainable investments[18] .

Recommendation #3.1 *[short term]* :

[KPI 1: Amount and proportion of business volume to which an exclusionary policy applies (respectively, in €bn and % of total business)

For any exclusion policy (particularly sectoral or normative) relating to environmental, social and/or societal issues, **the SEC recommends that the existing indicator be supplemented** with the following information, to allow comparison and detailed analysis of the robustness of the exclusion policies implemented and thus attest to their potentially transformative component:

- Indicate the amounts for which **non-application (exemption, breach) of the policy has been** observed.

- Specify the "activity" metric (assets under management, financing, on-balance sheet assets covered, off-balance sheet activities, investments, etc.), which should be chosen according to its relevance to the relevant business line. In this context, and in order to achieve optimal consistency with the Taxonomy Regulation and Annexes III to X of Delegated Regulation 2021/2178[19] , the SEC recommends that this metric be established taking into account, at a minimum[20] :
    - For entities affiliated with the Association Française de Gestion (AFG) and FI, total assets under management, excluding exposures to central governments, central banks and supranational issuers;
    - For entities affiliated with the FBF, all on- and off-balance sheet exposures ;
    - For entities affiliated with the FA :
        - For assets/investment activities: all direct and indirect investments (collective investment schemes, participations, loans and mortgages, tangible and intangible assets).
        - For liabilities/underwriting business: all "gross premiums written" collected on behalf of non-life insurance business
    - For entities affiliated with the ASF, total assets under management, total on- and off-balance sheet exposures and/or any other metric representative of the relevant business *.

[18] Busch, T., v. Hoorn, V., Stapelfeldt, M., Pruessner, E. (2022), "Classification Scheme for Sustainable Investments Accelerating the just and sustainable transition of the real economy", Eurosif, Universität Hamburg, White Paper

[19] Delegated Regulation EU 2021/2178

[20] This list is not exhaustive and should be supplemented with other relevant financial elements and metrics as appropriate.

Furthermore, the SEC notes that it would be more accurate to use the term "exclusion policies" (which can be sectoral or normative, for example), rather than "sectoral policies", which has a more restrictive connotation, i.e. limited to "sectors of activity".

NB: The SEC is aware that the ASF groups together non-homogeneous entities and that it is impossible to publish a single, unrepresentative aggregate indicator.

Remuneration

Recommendation #3.2 *[medium term]* :

[new] KPI 2: Average share of remuneration (as % of total remuneration) indexed to the sustainability / ESG performance of products, services and assets provided, managed and/or owned by the entity.

In line with European and French regulations[21] , the SEC recommends to all federations the publication of a new indicator, aimed at reflecting **the average share of total remuneration that is linked to the sustainability** (or "ESG") **performance of the financial products and services provided and/or managed by the entity**.

This indicator should :

- To be published for 1. **executive managers**[22] ; and 2. **employees involved in the design, management, monitoring, marketing or promotion of the entity's financial products and services.** All employees in the above categories should be included in the calculations (including those whose remuneration is not indexed to such criteria[23]).
- Indicate the breakdown, in %, between **short-term** remuneration (fixed and variable salaries) and **medium/long-term** remuneration (bonuses, profit-sharing, etc.).

Finally, the federations could also provide qualitative feedback on the **sustainability criteria** indexed to remuneration, based in particular on the materiality exercise which has been carried out.

21 (1) Regulation "SFDR" 2019/2088 of the European Parliament and of the Council - Article 5; (2) Decree No. 2021-663 of 27 May 2021 issued in application of Article L. 533-22-1 of the Monetary and Financial Code, pursuant to Article 29 of the Energy and Climate Law - Paragraph 3° b

22 Chairman and Chief Executive Officer, Chief Executive Officer, Deputy Chief Executive Officer, members of the Executive Committee, Executive Vice-President(s), Director(s)

23 All employees in the categories mentioned should be included in the calculation of the average share of remuneration indexed to such criteria, even for those whose remuneration is not indexed to them (in which case 0% will be counted for them). The indicator will therefore accurately reflect the average share of remuneration indexed to these criteria for all relevant employees.

Engagement / dialogue (incl. escalation process)

Finding:

Engagement or shareholder dialogue is defined as a medium/long-term process for an investor to influence the behaviour of companies in which they invest (or plan to invest) by interacting with them[24] . The goals of engagement can cover increased disclosure of extra-financial performance, improved ESG practices, or the advancement of a sustainability outcome [25][26] . By reflecting a willingness to change corporate practices motivated by a sustainability objective, shareholder engagement can contribute to the transformation of the activities of real economy actors, through the impact of the investor/financier on the invested/financed entities; however, this process does not allow for the inference of a direct impact of the investor/financier on the reduction of environmental pressures and/or on the improvement of social and societal indicators/factors [27][28] .

In addition, in order to provide exhaustive coverage of the business lines represented by the OFD, the term "engagement" or "dialogue" should be extended to include banking activities. Indeed, although the term "engagement" is traditionally assimilated with disintermediated/non-banking financing players, a growing number of banking institutions now have departments dedicated to engagement, support and advice on ESG issues for their clients.

In this respect, the engagement indicator published by the AFG and FA highlights a relevant lever to participate in the transformation of real economy players. However, it focuses solely on ESG integration within institutional commitment and voting policies. These policies measure *ex ante* means, not *ex post* results (the vote expressed *in fine*), which strongly limits the transformative scope of the indicator currently published.

Recommendation #3.3 *[medium term]* :

The SEC recommends eliminating the existing indicator and, by creating new indicators, reinforcing the measurement and publication of engagement and dialogue (in particular with shareholders, but also with entities financed or advised by banking institutions), the tabling of resolutions, and voting in general meetings.

24 GSIA (2021), "Global Sustainable Investment Review 2020

25 Eurosif Report (2021), "Fostering Investor Impact Placing it at the Heart of Sustainable Finance

26 PRI (2022), "Principles for Responsible Investment", Reporting Framework glossary

27 Kölbel et al (2020), "Can sustainable investing save the world: reviewing the mechanisms of investor impact".

28 Caldecott, B.L., Clark, A., Harnett, E., Koskelo, K., Wilson, C., & Liu, F. (2022), "Sustainable Finance and Transmission Mechanisms to the Real Economy", University of Oxford Smith School of Enterprise and the Environment Working Paper 22-04

[new] KPI 3: Proportion of investee companies and/or companies benefiting from the provision of a financial product or service with which a process of engagement or dialogue in relation to environmental, social and governance issues is undertaken (as a % of the total number of relevant companies).

Recommendation #3.4 *[medium term]* :

[new] KPI 4 *[on the indicator of proportion of entities subject to engagement/dialogue, reported via KPI 3]*: ***Proportion (%) of entities that are subject to requests from financial institutions and, where appropriate, have complied with these requests or been subject to an escalation process.***

This indicator should reflect the following three complementary components (which add up to 100%):

- (1) Percentage of entities with which the financial institution has initiated a dialogue without making a specific request;
- Among the entities for which the financial institution has made specific requests:
  - (2) Percentage of entities working on/having met the requests ;
  - (3) Percentage of entities that have not met requests and are subject to an "escalation" process.

    Ideally, the SEC recommends detailing this set by distinguishing between entities that have been subject to :
    - (i) a cessation of the acquisition of new securities / a lack of new equity investments / a cessation of the provision of new financing, financial products and/or services to the company;
    - (ii) a gradual disinvestment from the company / a tightening of the conditions of access to finance, products and/or financial services provided to the company;
    - (iii) a withdrawal from all or part[29] of the company's activities / a complete and immediate cessation of financing, products and/or financial services provided to the company.

NB: For banks, this indicator could also include the number of negative credit decisions made in relation to financing for activities that are unfavourable to environmental, social and governance issues.

In order to introduce the two indicators mentioned above, the SEC recommends that the OFD and the federations accompany this set of indicators with explanations of the processes of engagement and dialogue, and in particular of their transformative impact, which requires long-term work.

[29] Through the disposal of one or more specific activities of the joint venture

In this respect, the SEC recalls that the figures published in this section only partially reflect the efforts made by the institutions initiating the commitment, and that its full appreciation is made in a qualitative manner, which is outside the scope of publication of the OFD.

Resolutions

Finding:

Resolution filing initiatives, if they are part of a collective dynamic, can be an effective lever for transforming the practices of the invested/funded entities.

Recommendation #3.5 *[medium term]* :

[new] KPI 5: Proportion of financial institutions that have at least (1) tabled a resolution* or (2) joined a collective initiative to table a resolution in favour of environmental, social and governance issues (as a % of total financial institutions)

The SEC recommends the publication of the proportion of financial institutions that have tabled a resolution or joined a collective initiative to table a resolution in favour of environmental, social and governance issues.

***NB 1: In the case of FI affiliates, this refers to the inclusion of resolutions on the agenda of the board of directors or supervisory board**

****NB 2: Although this indicator is traditionally applied to disintermediated/non-bank financing players, it can also be applied to banks in the case of ownership of voting securities.**

Vote

Finding:

The indicator currently published on this subject refers to the integration of ESG criteria in the voting policy. As indicated above (section "shareholder engagement"), this *ex-ante* integration does not prejudge the final vote that will be cast by the financial institution.

Recommendation #3.6 *[medium term]* :

[new/replaces existing KPI] KPI 6: Breakdown of votes ("for", "against", "abstention") on shareholder resolutions supporting environmental, social and governance issues, as a % of total votes cast

The SEC recommends, as an alternative to the currently published indicator, the publication of an indicator that reflects explicit support (or opposition) on the part of financial institutions to shareholder resolutions that are favourable to environmental, social and governance aspects and more ambitious than the company's current policy.

***NB: Although this indicator is traditionally applied to disintermediated/non-bank financing players, it can also be applied to banks in the case of ownership of voting securities.**

- *Sub-theme #2: "responsible products*

AMF classification

Finding:

This indicator is currently published by the AFG, in terms of the amount and proportion of assets under management corresponding to "category 1 of position-recommendation 2020-03" of the French financial markets authority (AMF)[30] , in relation to the total assets under management by the federation in 2020.

Recommendation #3.7 *[medium term]* :

[existing/to be completed] KPI 7: Amount and proportion of AuM, assets or products distributed associated with category 1 of the "position-recommendation" issued by the AMF (in €bn and as a % of total AuM, assets or products distributed, respectively), broken down by "dominant strategy"[31] .

The SEC recommends maintaining the existing indicator - which stems from recommendations by the Autorité des Marchés Financiers (AMF)[32] - but suggests that this indicator be accompanied by explanations of the transformative potential of each of the associated "dominant strategies". The explanations should focus in particular on the **level of contribution of each strategy to the transformation of financial practices and flows, and/or according to their level of contribution to**

[30] Autorité des Marchés Financiers (AMF), POSITION - RECOMMENDATION, DOC-2020-03 (2020), p. 1-3: "only approaches with a significant commitment can present extra-financial criteria as a central element of the product's communication, for example in its name". In this context, the "category 1" mentioned refers to approaches based on a significant commitment in management.

[31] See *OFD* - "Integrating extra-financial criteria into traditional analysis": the term "dominant strategies" is used by the AFG.

[32] Autorité des Marchés Financiers (AMF), POSITION - RECOMMENDATION, DOC-2020-03 (2020), p. 2.

the transformation of the real economy. This classification should be based on the existing literature [33][34] [35] [36] .

In addition, the SEC considers that **this indicator could be published by all federations**. **The AMF's position-recommendation also concerns managers and distributors of certain collective investment schemes authorised to be marketed in France to non-professional investors, which may include players in the banking and insurance networks**.

Consequently, the metrics used (assets under management, balance sheet assets covered, amounts related to distributed products) will have to be adapted according to its relevance to the relevant business line.

SFDR Regulation

Finding:
This indicator is currently published by the AFG and reflects the provisions of the European Regulation (EU) 2019/2088, known as the "SFDR", by virtue of its Articles 8 and 9[37] .

However, the indicator as currently published is part of a regulatory context that still seems too unclear as to the scope of the provisions relating to the relevant articles[38] . Indeed, the outstanding amounts and corresponding products claiming to be covered by "article 8 or 9" of the SFDR are the result of self-declaration by financial institutions, and the provisions contained in these articles do not systematically reflect responsible investment or sustainable investment practices[39] . Therefore, compliance with the "Article 8" and/or "Article 9" provisions of the SFDR regulation is not necessarily, at present, synonymous with a transformation of financial practices or flows, nor with a

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33 Eurosif Report (2021), "Fostering Investor Impact Placing it at the Heart of Sustainable Finance

34 Caldecott, B.L., Clark, A., Harnett, E., Koskelo, K., Wilson, C., & Liu, F. (2022), "Sustainable Finance and Transmission Mechanisms to the Real Economy", University of Oxford Smith School of Enterprise and the Environment Working Paper 22-04

35 Kölbel, Julian and Heeb, Florian and Paetzold, Falko and Busch, Timo (2019), 'Can Sustainable Investing Save the World? Reviewing the Mechanisms of Investor Impact". Available at SSRN: https://ssrn.com/abstract=3289544 or http://dx.doi.org/10.2139/ssrn.3289544

36 IMP (2019). "Investor contribution in public and private markets: Discussion document". Impact Management Project.

37 Regulation EU 2019/2088 of the European Parliament and of the Council, the so-called *Sustainable Finance Disclosures Regulation* or "SFDR", pp. 11-12: Article 8 of the SFDR sets out provisions on "transparency of the promotion of environmental or social features in published pre-contractual information"; Article 9 of the SFDR sets out provisions on "transparency of sustainable investments in published pre-contractual information".

38 Speech by the AMF Chairman (June 2022) - *AMF Scientific Advisory Board Conference: "Non-Financial Reporting in Europe*

39 European Commission - Annex: "Question related to Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (Sustainable Finance Disclosure Regulation 2019/2088)", pp. 7-8 (July 2021)

transformation of the real economy compatible with the objectives of ecological transition and/or sustainable development.

Indeed, a product whose characteristics comply with the provisions of Article 8 could adopt a more robust approach to sustainable investment than that undertaken by a product complying with the provisions of Article 9. This difference in ambition and performance is currently not regulated by the SFDR. The risks of greenwashing are therefore real.

In this respect, the SEC recognises that the provisions relating to Articles 8 and 9 should be the subject of further work by the European Commission, both at the level of the regulatory framework - adding safeguards or minimum requirements such as, among others : clarification of the investment universe; pre-requisites concerning the framework of the notion of commitment; minimum performance thresholds for the "sustainable" (from an environmental point of view) part within the meaning of the European taxonomy[40] ; exclusion thresholds - and current disclosure practices - by adding, for example, information that would clarify the disclosure relating to Articles 8 and 9, such as the "sustainable investment" part within the meaning of the European taxonomy. These elements could be specified on the basis of the provisions of the technical regulatory standards adopted in April 2022 by the European Commission[41] .

Recommendation #3.8 *[medium term]* :

[KPI 8: Amount and proportion of assets under management, unit-linked assets or products marketed or distributed corresponding to the provisions of Articles 8 and 9 of the EU SFDR (respectively, in bn€ of assets/assets covered and as a % of total assets/assets under management/assets marketed/assets distributed, detailed by category of article)

In this context, the SEC recommends maintaining the existing indicator, which highlights the current regulatory exercise, but invites the financial federations to accompany the publication of this indicator with the following elements

- Disclose within each "Article 8" and "Article 9" product category the share of environmentally sustainable investments as defined in the Taxonomy Regulation ("aligned" share)[42] .
- Indicate in the contextual information that "Article 8" products are not systematically linked to an ESG, responsible investment or sustainable investment objective;

[40] Regulation EU 2020/852 of the European Parliament and of the Council

[41] Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022 supplementing Regulation (EU) 2019/2088 of the European Parliament and of the Council with technical regulatory standards (August 2022)

[42] Part defined as "aligned" within the meaning of Delegated Regulation 2021/2178 on Article 8 of the Taxonomy Regulation 2020/852.

- Pending regulatory clarification, delete any reference to "responsible investment", as this concept does not appear in the SFDR.

Furthermore, the SEC **recommends that this indicator be published by FA and FI** - whose affiliates are subject to SFDR -, **but also by the FBF**: indeed, although a large majority of actors and activities represented by the FBF are excluded from the perimeter of entities and activities subject to the European regulation, they will be impacted by the distribution of "Article 8" and "Article 9" products, through the delegated regulation establishing sustainability preferences[43] taken in application of "MiFID II".

Labelled funds

Finding:

An indicator linked to the funds labelled "ISR" (State label managed by the Ministry of Finance), "Greenfin" (State label managed by the Ministry of the Environment), "Finansol" (independent label created by the Finansol association), as well as to other European public or private labels for financial products, is published by the AFG, the FBF and FA.

Nevertheless, the SEC recommends a different publication from what is currently practised, insofar as these indicators do not systematically attest to the transformation of practices and financial flows in favour of environmental and/or social objectives. Indeed, of the three labels that are published, not all promote sustainable investment and they do not limit or prohibit the labelling of a fund that invests, in particular, in activities that are harmful to the environment[44] . In this context, it seems difficult, if not impossible, to consider that labelled assets systematically make a positive contribution to the ecological transition. It therefore seems necessary to clarify and verify the characteristics (environmental and/or social) promoted or not by each label.

In addition, despite the existence of a common metric, the indicator is reported under different parameters. These differences do not seem to be justified by the specific characteristics of each business line. For example, the banking business publishes the amounts invested and the number of relevant labelled funds, on a European basis; the asset management business focuses on the "amounts invested in labelled funds" of the assets under management, as well as the number of corresponding labelled funds, including European labels; finally, the insurance business communicates on the "amounts invested in labelled units of account" but does not publish the number of relevant funds , and limits itself to the scope of French labels. On the other hand, the SEC notes the good practice applied by the AFG concerning the disclosure of the number of funds and the associated amounts.

[43] Delegated Regulation 2021/1253 of 21 April 2021

[44] For example, to date (October 2022), the SRI label does not exclude fossil fuels.

	Legend 1[45]	Legend 2[46]	Geographical scope of the relevant labels
AFG	"Amounts invested in labelled funds	"Certified stocks".	Europe
FBF	"Amounts invested [...] in label-certified funds	N/A *(a single graph is presented)*	Europe
FA[47]	*"Amounts invested* in labelled unit-linked funds	"Responsible, green and solidarity-based *unit-linked* funds".	France

Recommendation #3.9 *[short term]* :

[KPI 9: Amount and proportion of labelled funds marketed or distributed, or assets invested or managed in labelled funds (respectively in €bn and as % of total assets/assets under management/assets marketed/assets distributed)*

In this context, and following the example set by the AFG, the SEC recommends to:

- Clarify the description, objectives and characteristics promoted by each label, indicating, for example, what it does and does not allow;
- Highlight the amounts and proportions of labelled assets. The number of labelled funds, presented as an absolute value and without any relation to total assets under management, does not seem to add any value to the information provided. Moving it to the back, in favour of assets under management, would improve the readability of the information published;
- Harmonise the contextual information accompanying published data (e.g. terms used in legends);
- Agree on a common geographical scope (France or Europe) and detail the list of relevant labels.

***NB: In this context, the metric used should be adapted according to its relevance to the relevant business.**

Bonds and loans

45 Corresponding to the 1st graph published in the dedicated section on the OFD website
46 Corresponding to the 2nd graph published in the dedicated section of the Observatory's website
47 The difference in terminology can create confusion about whether the data published refers to amounts invested directly by insurers, or whether it refers to unit-linked assets invested by their customers.

<u>Finding:</u>

The indicator currently published on this topic refers to structured or underwritten bonds ("green", "sustainable", "social", "sustainability backed", "transition").

However, these amounts are not systematically compared with the total volumes of structured / subscribed bonds. The information published does not therefore make it possible to assess the relative importance of these instruments in relation to the total transactions and amounts managed by the financial institutions.

In addition, several studies point to the risk of the lack of transformative and "additional" character of green and sustainability bonds (or "SLBs[48] "), as well as the induced risk of greenwashing [49][50] [51] .

Finally, the current indicator focuses on bonds and omits loans, which constitute a significant proportion of debt instruments, whereas bank credit is a substantial contributor to the financing of the real economy, especially at the French and European levels [52][53] [54] .

In this context, and in order to best protect against the above-mentioned risks, the SEC recommends:

<u>Recommendation #3.10 *[medium term]* :</u>

[existing/to be completed] KPI 10.1 - Bonds: amount and proportion of bonds structured or underwritten that promote "green", "sustainable", "social", "sustainability backed"[55] and/or "transition" features (respectively, in bn€ and as % of total amounts for bonds structured or underwritten)

The SEC recommends that :

- Express the indicators for "green", "sustainable", "social", "sustainability-backed" and/or "transition" bonds as **a proportion (%) of the total amount of bonds underwritten or structured** (depending on the business line), as currently published by the AFG;
    - Ideally, distinguish between bonds whose coupons are backed by sustainability / ESG criteria and those that are not;

48 Sustainability-linked bonds

49 Yeow and Ng (2021), "The impact of green bonds on corporate environmental and financial performance", *Emerald Publishing Limited*

50 Ekeland and Lefournier (2019), "The green bond: homeopathy or incantation? "

51 Freeburn and Ramsay (2020), "Green bonds: legal and policy issues", *Capital Markets Law Journal* :

52 Banque de France (2021), "Le financement des entreprises en sortie de crise": French companies are highly dependent on bank financing; in particular SMEs, whose share of bank credit in their debt represented 85% in 2019 (or even 95% if leasing is taken into account).

53 Bruegel (2020), "Boosting the resilience of Europe's financial system in the coronavirus crisis".

54 OECD (2022), "Financing SMEs and Entrepreneurs 2022: An OECD Scoreboard".

55 In the sense of "sustainability-linked".

- Include a **systematic reference to the standard(s), framework(s) and/or principle(s) followed by the obligation**. In the absence of a standard, framework or principle, the SEC recommends indicating that this is an arbitrary classification.

[new - specific to FBF affiliates] KPI 10.2 - Loans: ***amount and proportion of loans granted that promote "green", "sustainable", "social", "sustainability objectives[56] " and/or "transition" features (respectively, in €bn and as a % of the total amounts of loans granted)*.***

- Complement the current indicator on bonds **with an indicator on** "green", "sustainable", "social", "sustainability-based" and/or "transition" **lending** by financial institutions, **showing their proportion (in %) of total lending**;

The publication of data could be based on those currently disclosed by the ASF within the "Transition to a low-carbon economy" theme.

NB: The SEC does not recommend a single indicator for all federations. Each federation should adapt its publication according to the relationship between the debt instruments mentioned (bonds/loans) and the business line.

Financial inclusion

<u>Finding:</u>

An indicator on financial inclusion is published by the FBF and highlights loans granted to Social and Solidarity Economy (ESS) enterprises, as well as professional and personal microcredits.

This social indicator echoes the "just transition" imperatives recently put forward by international bodies [57][58] [59] as well as by the Place de Paris[60] . Similarly, access to financial services is considered a factor of progress and growth defined by several United Nations Sustainable Development Goals[61] .

However, this indicator does not include a definition of financial inclusion, which may imply that financial inclusion is limited to the promotion of ESS and micro-credit. Furthermore, the economic

56 Same as previous ref.

57 International Labour Organization (2022), "G20 Sustainable Finance Working Group Input Paper - Finance for a Just Transition and the Role of Transition Finance".

58 IPCC (2021), "IPCC WGII Sixth Assessment Report: Summary for Policymakers", pp. 7, 32

59 OECD (2021), "The inequalities-environment nexus: Towards a people-centred green transition", OECD Green Growth Papers, No. 2021/01, OECD Publishing, Paris, https://doi.org/10.1787/ca9d8479-en

60 Investors for a Just Transition - Finance for Tomorrow (2021)

61 United Nations, *Sustainable Development Goals*, targets 8.3 and 9.3

sectors covered by the category "ESS" are not specified. Also, no definition of ESS is provided.

Recommendation #3.11 *[medium term]* :

[new or existing to be completed, depending on the trade] KPI 11 - Financial Inclusion

The SEC recommends that :

[For entities that already publish a financial inclusion indicator - the FBF]

1. **Define and detail more precisely the terms "financial inclusion"** and "ESS". In doing so, federations could draw on the definitions provided by the World Bank[62] and/or, on a French scale, the Banque de France[63] ;
2. **Specify the sectors of economic activities covered** by the loans granted to ESS actors.

[For those entities that do not publish a financial inclusion indicator and to which such an indicator is applicable, i.e. FA and ASF]

- **Establish and/or promote a specific indicator on financial inclusion.** Indeed, the insurance and financing businesses are likely to offer financial inclusion products in the following areas
    a. Financial products and services, including
        i. Micro-insurance (or "inclusive insurance") / micro-credit ;
        ii. More generally, adapted/preferential financial services for people in a situation of financial difficulty;
    b. Non-financial services, including
        i. Advice and technical expertise for financially vulnerable clients;
        ii. Financial education and awareness raising.

In all cases, and in line with the cross-cutting recommendations mentioned in this document, the SEC recommends that published data be expressed as a proportion (%) of the total amount of loans granted/services provided.

NB: The SEC does not recommend a single financial inclusion indicator for all federations. Each federation should adapt its publication according to the relationship between the financial inclusion products mentioned and the trade carried out.

[62] World Bank (2022), "Financial Inclusion".
[63] Banque de France (2022), "Financial inclusion: what is it?

Recommendation #3.12 *[short term]* :

ICP: "Membership of international coalitions/initiatives

The SEC recommends the elimination of this indicator, particularly because of questions surrounding the concept and actual transition funding implications of joining coalitions or initiatives.

Indeed, membership (of a coalition or an initiative) does not prejudge the degree of involvement of a financial institution in ESG issues. In this respect, recent studies have highlighted the limits of voluntary initiatives by financial players[64] .

Therefore, the SEC invites the federations to focus their efforts on the indicators proposed in these recommendations.

Section #4: Ensuring the most comprehensive trade publication possible

Finding:

Some business lines do not currently publish any data on the management and supply of responsible products, despite the implications for some of their activities. In particular, specialised finance institutions do not publish ESG data for their consumer finance, leasing, housing finance, and/or other financial services businesses. Similarly, private equity entities do not publish any data on responsible management, even though these businesses are able to use the levers mentioned in the proposed recommendations on aspects such as commitment, exclusion policies, voting, AMF position-recommendation 2020-03, and the alignment of investments with the provisions of Articles 8 and 9 of Regulation 2019/2088 "SFDR".

Objective of the SEC :

This recommendation aims to ensure that federations publish the indicators applicable to them in a comprehensive manner.

The table below summarises the division into two sub-themes ("entity practices and strategies"; and "products and services") and the 11 KPIs attached to them. The SEC has identified 6 indicators to be published as a priority (in green in the table below) by virtue of their transformative aspect of the activities of OFD member federations. The SEC considers that the communication of these "main" indicators does not exempt the publication of the other indicators which can provide a complementary vision of the federations' commitment to ESG objectives.

[64] Finance Watch (2022), *The problem lies in the net: How finance can contribute to making the world reach its greenhouse gas net-zero ta*

Sub-theme #1	entity" practices and strategies	AFG	FA	FBF	FI	ASF
ICP 1	Exclusion policy	X				
ICP 2	Remuneration	X				
ICP 3	Engagement / Dialogue	X				X
ICP 4	Escalation process	X	X	X	X	X
ICP 5	Resolutions	X	X	X	X	X
ICP 6	Vote	X	X	X	X	X
Sub-theme #2	**"products and services**	**AFG**	**FA**	**FBF**	**FI**	**ASF**
ICP 7	Position - AMF recommendation	X	X	X	X	X
ICP 8	SFDR Regulation (art. 8 and art. 9)	X	X	X	X	X
ICP 9	Labelled funds	X				X
ICP 10	Bonds and loans	X				
ICP 11	Financial inclusion	N/A	X	X	N/A	X

X	*Recommended publication*
X	*Recommended publication with possible trade exemptions (to be justified)*

V. Recommendations for indicators related to the Transition to a Carbon Neutral Economy

a. Introduction

The SEC has taken into account the fact that the analysis and evaluation of the transition of financial actors to a "carbon neutral economy" is still a recent and evolving field. The very concepts related to "carbon neutrality" are gradually being clarified and specified. The SEC understands "carbon neutrality" to be consistent with the work of the IPCC, i.e. a situation where residual CO_2 equivalent emissions are permanently sequestered so that the level of concentration in the atmosphere is stabilised. The application of this concept at company level gives rise to different debates and definitions which are not the subject of this document (see below).

Concepts related to carbon neutrality

To illustrate the difficulties of defining "carbon neutrality" at the corporate level, it is useful to refer to the various concepts specified by the United Nations "Race to Zero" partners in their lexicon[65] :

- Net Zero: Individual actors have reached a "net zero" situation when they have reduced their GHG emissions according to a science-based trajectory, and their residual emissions are fully offset over a specific period of time and on a permanent basis, within their value chain or through the acquisition of valid offset credits.

- Carbon neutral: actors are considered carbon neutral when the GHG emissions of these actors are fully "offset" either by a reduction of CO_2 from these actors or by a removal of CO_2 produced exclusively by these actors so that the net contribution of these actors to the overall CO_2 emissions is zero regardless of the period considered.

Many public and private initiatives have recently been developed to promote the goal of carbon neutrality. For example, the aforementioned "Race to Zero" is a global campaign by the United Nations (launched ahead of COP 26 in 2021) to engage businesses, cities, regions, investors and universities in the drive towards zero carbon emissions by 2050. Beyond this, the OECD identifies a large number of initiatives recently developed to promote "climate alignment" of financial and non-financial companies[66] (see below).

Climate alignment initiatives (OECD census)

[65] United Nations, Race to Zero Lexicon, April 2021

[66] OECD Environment Working Papers No. 200 "Assessing the climate consistency of finance: Taking stock of methodologies and their links to climate mitigation policy objectives" - October 2022

The initiatives identified take the form of coalitions of stakeholders brought together voluntarily, frameworks providing general recommendations or methodologies for achieving certain standards or objectives. More than twenty initiatives have been identified to date. Among the most recent are initiatives created to promote "Net Zero":

- The Glasgow Financial Alliance for Net Zero created in 2021 brings together 7 alliances of financial players (Net Zero Asset Managers initiative (NZAM), Net-Zero Asset Owner Alliance (NZAOA), Net-Zero Banking Alliance (NZBA), Net Zero Financial Service Providers Alliance (NZFSPA), Net-Zero Insurance Alliance (NZIA), Net Zero Investment Consultants Initiative (NZICI) and Paris Aligned Investment Initiative (PAII)).

- SBTi Financial Institutions Net Zero, which applies the "science-based" approach developed for non-financial companies to financial institutions.

The SEC stresses the need for the OFD to provide a comprehensive view of the transformation undertaken by financial actors to support the transition to a carbon neutral economy. To this end, it considers that relevant information should be provided on several aspects:

- The strategy of the actors, in particular the objectives set with quantitative targets to be reached and dates to be respected;

- The policies implemented, the instruments used (in particular indicators and methodologies) and the means mobilised to achieve the objectives set. In this respect, the sectoral policies implemented by the financial actors, the commitment policies implemented with their modalities (dialogue, voting policy, escalation mechanism) but also the human resources mobilised and the internal incentive policies implemented (in particular remuneration policies) are relevant information on the real commitment of financial actors.

- The transformation effectively undertaken by the actors of their activities, i.e. the effective reorientation of financing flows and financial services carried out by the financial actors in application of the strategy decided upon. From this point of view, the information communicated must cover the financing of sustainable activities, activities in transition as well as the most emitting activities which are likely to decrease significantly, or even disappear, at the end of the transition.

- While all of this information seems relevant to the SEC for the proper information of OFD users, it is not mandatory that it all be included in the OFD section dedicated to the transition to a carbon neutral economy. It was therefore recommended that some of this information (for example, that relating to policies implemented or incentive policies) be gathered in the section relating to ESG practices.

The SEC also stresses that the OFD data should be assessed against the Sixth Assessment Report of the Intergovernmental Panel on Climate Change - IPCC (2022) - which explains why limiting the increase in global warming to 1.5°C by 2100 should be the preferred objective - and the IEA's "Net Zero by 2050" scenario (2021). It is in particular from this scientific data that the SEC has based its recommendations on the scenarios to be retained, favouring scenarios aiming to limit global warming to 1.5°C and respecting certain conditions (including: limited overshoot, moderate use of techniques to recover and store the CO_2 emitted, etc.).

Finally, it is important to stress that the application of carbon neutrality concepts to companies is taking place in a regulatory framework that is evolving rapidly in the European Union (implementation or finalisation of various texts including the European regulation on the taxonomy of sustainable activities, the Sustainable Finance Disclosure Regulation (SFDR) or the Corporate Sustainable Reporting Directive (CSRD)).

In addition, key analytical work is underway both at the international level (e.g., G20 Sustainable Finance Working Group, private initiatives such as GFANZ and SBTi) and at the national level (e.g., Finance ClimAct's work based on a questionnaire to market participants[67]) to improve indicators and methodologies for monitoring the transformation of the activity of financial players regarding the needs of the transition to a carbon neutral economy.

In this highly evolving context, the SEC has chosen to publish a first series of recommendations which are necessarily partial - as they are based on the elements of reflection and the regulatory provisions currently known. This work will have to be completed by a second series of recommendations to be published later.

The paper first looks at indicators relating to the objectives and instruments put in place to facilitate the transition and then at indicators to assess the transformation of the activities of financial actors.

b. Recommendations

In order to best present the challenges of the transition to a carbon-neutral economy for all financial actors, the introductory section of this theme in the OFD must be revised and harmonised. These should be adapted to take into account the different types of financial actors reporting to the Observatory.

Recommendation #1:

The SEC recommends that the introductory section of the "Transition to a carbon neutral economy" theme be revised to expand on the issues and harmonise the presentation between the different categories of financial actors.

[67] https://observatoiredelafinancedurable.com/fr/presentation/actualites/lancement-dune-%C3%A9tude-finance-climact/

Part I: Recommendations on the goals and instrument used

As mentioned above, information is needed on the strategy of financial actors, but also on the policies implemented and the tools used. This first part of the recommendations therefore covers the objectives of the financial actors - in order to assess the transition strategies chosen - and the instruments used. However, the policies implemented are not addressed here as they are the subject of recommendations in the chapter on the integration of ESG issues.

In this category, the recommendations are mainly aimed at generalising and clarifying indicators already published by certain federations on the OFD website. The recommendations made in the following section are intended to be implemented in the short term by the financial actors (i.e. for the next collection of information).

Section 1: OFD Indicators for Carbon Neutrality Targets for Financial Actors

Findings on the existing situation

On the OFD website, two indicators focus on the targets set for the transition to carbon neutrality for financial actors. They are provided by the AFG and FA. The two indicators aim to measure the environmental transition objectives that the members of these federations have set for their investment portfolios.

The indicator published by the AFG corresponds to the share of management companies that have implemented alignment, neutrality or other environmental objectives[68] , in 2020. It is expressed as a percentage of management companies that are committed to one of the three types of objectives, out of all management companies.

The indicator published by FA shows the share of insurance organisations with carbon alignment or carbon neutrality targets in place in 2020. It is expressed as a percentage of insurance organisations committed to a carbon alignment or carbon neutrality target, across all entities.

Objectives :

The SEC recommends that the publication of an indicator expressing the proportion of financial players that have set targets for the transition to carbon neutrality be extended to all financial sectors, not just the financial management and insurance sectors. On the other hand, the SEC notes a lack of

[68] The "other objectives" include the following data:
- the calculation of the green intensity of the fund using the percentage of eco-activities defined by the Greenfin label, following the Climate Bond Initiative nomenclature
- calculations based on the "SmartforClimate" scoring model,
- the calculation of the Energy Transition Score, which is an internal score to assess an issuer's transition risk exposure and contribution to transition,
- calculations and targets based on the Net Environmental Contribution (NEC).

precision in the two existing indicators: for example, they do not present information on the reference scenario[69] , which makes their interpretation difficult.

The SEC therefore recommends that this indicator be generalised, with additional details on the data to be published. The indicator should :

- Identify the quantitative commitments made by the players in terms of alignment or carbon neutrality by 2030 (retained by Article 29 of the 2019 Energy-Climate Law) [70]
- Distinguish between financial actors according to the type of reference scenario used to set the quantitative target: the most ambitious scenarios (warming limited to 1.5°C, small overshoot, moderate use of negative emissions) and the other scenarios (maximum warming up to 2°C).

Recommendation #2:

The SEC recommends the publication of the following indicators:
- Indicator 2.1: number of actors in the federation that have set a quantitative target of alignment or carbon neutrality by 2030 in relation to a 1.5°C scenario that meets certain conditions (see below) and the share of these actors in the total financing of the federation's members.
- Indicator 2.2: Number of federation actors that have set a quantitative target of carbon alignment or carbon neutrality by 2030 compared to other scenarios (the maximum warming temperature of the scenarios considered should not exceed 2°C) and the share of these actors in the total funding of federation members.

Technical note:
Only 1.5°C scenarios that meet certain characteristics can be used for the calculation of indicator 2.1 - such as the IEA Net-Zero scenario, the IPCC C1 scenarios or any other 1.5°C scenario with no overshoot (i.e. with at least a 50% probability of limiting warming to 1.5°C in 2100) or little overshoot (i.e. limiting warming to 1.6°C with a return to 1.5°C by 2100 (due to low reliance on negative emissions).

Articulation with regulations

Article 29 of the Energy-Climate Law (LEC) requires the publication by the relevant actors of their alignment strategy with the long-term objectives of the Paris Agreement for investment and portfolio

[69] The term "baseline scenario" here refers to "possible climate changes throughout the 21st century as a function of greenhouse gas emissions and thus the evolution of human societies." Definition taken from the article "Where do the five new IPCC scenarios come from?" published on 14 September 2021 by Charlotte Vailles - I4CE.
[70] https://www.legifrance.gouv.fr/jorf/article_jo/JORFARTI000039355992

management activities. The implementing decree of 27 May 2021[71] specifies that the alignment strategy of financial actors must include in particular:

- A quantitative target to be reached by the year 2030. This target is to be reviewed every 5 years until 2050. It relates to direct and indirect greenhouse gas emissions[72] , expressed in absolute or intensity terms, compared to a baseline scenario. This quantitative commitment can be expressed as a measure of the implied temperature increase or as the volume of greenhouse gas emissions.
- Where the entity uses an internal methodology, elements on this methodology to assess the alignment of the investment strategy (general approach, portfolio coverage, time horizon, energy/climate scenarios selected, etc.).
- Quantification of results using at least one indicator.

In application of these regulatory provisions, all the relevant financial players [73] must publish a quantitative objective for 2030 to align with the Paris Agreement, specifying the reference scenario used. The SEC's recommendation aims to obtain aggregate data at the level of federations from the quantitative alignment commitments published under the current regulations, distinguishing according to the level of ambition of the reference scenario used by financial players to set their environmental targets. These regulatory provisions come into force for reporting in 2022 for the financial year 2021.

It is useful to recall that the implementing decree puts in place a reinforced "*comply or explain*" mechanism. It is therefore envisaged that financial actors will not publish all the information requested. In this case, the relevant entities must publish a "continuous improvement plan" which provides information on the improvement strategy, the concrete actions selected and the strategic and operational changes implemented to remedy the situation, with objectives and an implementation schedule.

Section 2: Indicators on instruments used to measure alignment

Finding:
An indicator on the share of banks using alignment measurement tools is currently provided by the FBF. However, the lack of precision in the indicator on the requirements retained by the alignment measurement tools identified makes it difficult to interpret. Furthermore, the publication of an indicator does not prejudge the level of alignment achieved, nor the use made of it by the entities that

[71] https://www.tresor.economie.gouv.fr/Articles/2021/06/08/publication-du-decret-d-application-de-l-article-29-de-la-loi-energie-climat-sur-le-reporting-extra-financier-des-acteurs-de-marche

[72] Definition of the different greenhouse gas emission scopes: https://www.territoires-climat.ademe.fr/ressource/42-14, website of the French Agency for the Environment and Energy Management and ADEME

[73] In particular, Article 29 LEC concerns portfolio management companies (management on behalf of third parties), insurance and mutual companies, reinsurers, provident institutions, credit institutions and investment firms providing management on behalf of third parties and investment advice.

publish it. Finally, alignment indicators are subject to criticism in terms of the assumptions on which they are based and their lack of homogeneity and, consequently, their incomparability.

Objectives :

Despite these various reservations, the SEC's recommendation is to generalise an indicator of this type for all financial sectors and to specify it to facilitate its interpretation. Indeed, the SEC considers that the use of such an indicator provides information on the involvement of the actor using it (the question of measuring alignment itself is addressed in recommendation 8 of this section).

The recommendation distinguishes between financial actors using an alignment measurement instrument according to the level of ambition of the reference scenario used:

- Actors carrying out an alignment measure against a 1.5°C scenario meeting the characteristics specified in the previous recommendation (the IEA Net-Zero scenario, the IPCC C1 scenarios or any other 1.5°C scenario with little or no overshoot and low reliance on negative emissions)
- Actors carrying out an alignment measure with another scenario (but leading to a maximum warming of 2°C).

Analysis of what financial actors are doing in this area shows that these alignment measures never cover total investments or financing (notably because of the limitations of the available methodologies and the unavailability of certain data). Furthermore, the scope of coverage is different across financial entities and is likely to improve over time. It is therefore essential that an indication is given of the scope covered at each reporting date (as a percentage of investments or financing granted) in order to be able to assess the actual extent of the implementation of the alignment measures.

In addition to the scope covered by this alignment measure in terms of outstanding amounts, it would also be very significant to provide information on the share of Scope 3 emissions[74] of the entities covered by the alignment measure. This data would make it possible to assess whether a broad scope covered in terms of outstanding amounts does not leave out activities with high emissions or, *conversely*, whether a relatively narrow scope in terms of outstanding amounts concerns a significant proportion of the entities' Scope 3 emissions.

The SEC also questioned the appropriateness of asking federations to publish information on the difference between the quantitative target set under the regulations and the observed level of the alignment indicator selected. At the level of an entity, the difference between the level of the alignment indicator and the target set to date makes it possible to assess the progress made by the entity. However, it appears that the aggregation at the level of federations of the gaps measured at the individual level would run into major difficulties given the heterogeneity observed at present (different targets, different reference scenarios, different perimeters covered by the indicators, etc.). Under these conditions, the aggregate measurement of the gaps would be particularly precarious and difficult to interpret. A reduction in this heterogeneity would be an essential prerequisite before considering an aggregate measure of variance.

[74] Scope 3 emissions of financial actors, i.e. Scope 1, 2 and 3 emissions of their counterparts (according to the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard)

<u>Recommendation #3:</u>

The SEC recommends that each federation publish the following indicators:

Indicator 3.1:

- number of actors carrying out and publishing a measure of alignment of their portfolio or financing to a 1.5°C scenario meeting certain conditions (see above)

- average percentage of the portfolio or financing covered by this alignment measure in relation to the total portfolio or financing of each relevant actor

- share of these actors in the total portfolio or funding of the federation's members.

Indicator 3.2:

- number of actors publishing an indicator of alignment with scenarios other than a 1.5°C scenario (but at most a 2°C scenario).

- average percentage of the portfolio or financing covered by this alignment measure in relation to the total portfolio or financing of each relevant actor

- share of these actors in the total portfolio or funding of the federation's members.

The SEC also recommends that the federations, as a second step, consider supplementing the scope of coverage in terms of stocks with information on the scope of coverage in terms of Scope 3 GHG emissions.

<u>Articulation with regulations</u> :
Like Recommendation 1, this recommendation should be linked to the regulatory requirements (in particular, the implementing decree for Article 29 LEC), which require the relevant financial actors (see above) to publish an indicator to measure the results achieved in relation to the quantitative alignment objective requested (see above) for investment and portfolio management activities.

As with the previous recommendation, the objective of the SEC is to obtain aggregate data at the level of the federations from the alignment indicators published by each reporting entity under the terms of the regulations in force, distinguishing between players according to the level of ambition of the reference scenario used to set their environmental targets. The regulatory provisions come into force for the publication of information to be made in 2022 on the 2021 financial year.

Regarding banks in particular, it should be noted that the EBA, in its draft technical rules for the implementation of ESG risk transparency rules published in early 2022[75] , requires the major banks[76] to publish information on their alignment metrics for the *banking book*. These metrics provide information on banks' Scope 3 GHG emissions (i.e. Scope 1, Scope 2 and Scope 3 emissions of their counterparties) in relative terms, defined on the basis of the sectoral alignment metrics established by the IEA for different sectors (e.g. total GHG on a physical quantity). Banks will also have to publish the gap, by sector, between the value of their alignment metric and the level expected in 2030 in the reference scenario.

The information on the alignment measure published by certain categories of actors is therefore likely to be significantly enriched. This development will necessarily lead to a revision of the SEC recommendations.

Section 3: Indicators on the measurement of climate risks achieved

Finding:

An indicator of this type is currently provided by FA: it makes it possible to assess the share of institutions according to the type of climate risk assessment they carry out. This indicator is admittedly imperfect - in that it provides no information on the methodologies used (which vary considerably) or on the results obtained (level of physical or transitional risks to which financial players are exposed). Nevertheless, it provides an initial assessment of the sensitivity of institutions to the problem of climate risks and the means put in place to measure them.

Objectives :

The recommendation aims to generalise the FA indicator to all financial sectors represented in the OFD in order to assess the means put in place by the different categories of financial actors to measure climate change risks (physical, transition or liability risks).

It is based on the new regulatory provisions which stipulate that financial players must from now onwards publish information on their climate risk measurement and management systems (transition, physical and liability risks) (cf. decree implementing article 29 of the LEC). However, climate risk methodologies currently focus mainly on transition and physical risks, with a virtual absence of methodologies for assessing liability and litigation risks[77] .

The SEC is aware of these difficulties, which therefore lead to delaying the publication of information on the risk of liability and litigation to a more distant horizon. Nevertheless, the SEC prefers to remain

[75] "EBA final draft Implementing Technical Standards on Pillar 3 disclosures on ESG risks (January 2022), available here: https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Draft%20Technical%20Standards/2022/1026171/EBA%20draft%20ITS%20on%20Pillar%203%20disclosures%20on%20ESG%20risks.pdf

[76] "large institutions which have issued securities that are admitted to trading on a regulated market of any Member State"

[77] https://www.ngfs.net/sites/default/files/medias/documents/climate_related_litigation.pdf

in line with the more demanding French regulatory provisions, considering that this regulatory requirement will contribute to the awareness of financial players of the fact that this risk is already materialising and that they therefore need to equip themselves with assessment tools. It is likely that rapid progress will be made in this area.

Recommendation #4:

The SEC recommends publishing the distribution of financial actors according to the nature of the climate risk assessments in place, indicating the percentage of actors that :

1. do not assess climate risks (beyond, where appropriate, measuring their exposure to these different risks)

2. conduct a qualitative assessment

3. calculate a score

4. conduct a quantitative assessment of the financial impact of climate risks.

The indicator should distinguish between transition risks, physical risks and, as far as possible, litigation or liability risks related to climate change.

Articulation with regulations :

The SEC recommendation builds on existing regulations by requiring the aggregation of individual data to be published by each actor.

Indeed, the implementing decree of Article 29 LEC requires that the relevant financial actors disclose, for their investment or portfolio management activity, information relating to "the approaches to taking account of environmental, social and governance quality criteria in risk management". It specifies that the disclosure should include physical, transition and liability risks related to climate change. In particular, the information must cover :

- The "process for identifying, assessing, prioritising and managing risks related to the consideration of environmental, social and governance criteria and how the risks are integrated into the entity's conventional risk management framework".
- A description of the main risks (characterisation of the risks, typology and descriptive analysis of the risks, particularly physical, transitional and litigation or liability risks related to environmental factors, a quantitative estimate of the financial impact of the main environmental risks, etc.). The decree specifies: "*in the event that a qualitative statement is published, the entity shall describe the difficulties encountered and the measures envisaged to assess the financial impact of these risks*". Lastly, information is requested on changes in methodological choices and results.

On the basis of the information published to meet these regulatory obligations, the federations are asked to collect and aggregate the data relating to the four categories mentioned above. Insofar as some entities will not provide the corresponding data (see above the explanations relating to the reinforced "*comply or explain*" mechanism put in place by the implementing decree of Article 29 LEC), the implementation of the SEC's recommendation will make it possible to have a synthetic assessment of the evaluation mechanisms of each of the categories of climate risk put in place by the financial players.

These regulations will come into force for the reporting to be carried out in 2023 for the financial year 2022.

On the banks' side, the EBA in its draft technical rules[78] asks large European banks that are listed on an organised market to disclose information on their climate risks for their banking activities (exposures to high GHG emitting sectors under transition risks and exposures to extreme and chronic physical risks). It does not require the disclosure of quantitative information on an assessment of these risks, but qualitative information on the environmental risk management systems banks have in place (including methodologies and tools for identifying and measuring risks).

The SEC has taken a different approach. It does recommend publishing banks' exposures to high-emitting sectors to measure the environmental impact of the financing granted (see recommendation 5). However, regarding climate risks, its objective is to obtain information on the level of maturity of the risk assessment methodologies used by financial players. This approach is in line with the EBA's requests for qualitative information and this recommendation aims to summarise the level of maturity of the risk assessment tools used by financial actors.

Section 4: Indicators for measuring environmental impact

Finding:
There is currently no indicator provided on the OFD that measures the environmental impact of the activities of the different categories of financial actors. Only NGO estimates exist, but these are necessarily partial due to the absence of certain published information and therefore do not provide a sufficiently good understanding of the environmental impacts of financial actors.

Objectives :
The SEC considers that an indicator of this type, currently not proposed by any federation, is necessary to complete the information requested on climate risk assessment methods (see recommendation #4). Indeed, the double materiality approach - advocated by the European Union in terms of extra-financial reporting - requires financial actors to implement metrics regarding the environmental materiality of their investments and/or financing to complement the risk-based approach.

[78] "*EBA final draft Implementing Technical Standards on Pillar 3 disclosures on ESG risks*
https://www.eba.europa.eu/eba-publishes-binding-standards-pillar-3-disclosures-esg-risks

<u>Recommendation #5:</u>

The SEC recommends publishing aggregated information on the Scope 3 GHG emissions of the actors in each federation (i.e. Scope 1, Scope 2 and Scope 3 emissions of their counterparts). To this end, it recommends that the following indicators be put in place:

- Indicator 5.1: volume of counterparty Scope 1 GHG emissions and scope covered (weighted average percentage of portfolio outstanding and/or financing covered by this calculation)

- Indicator 5.2: Volume of counterparty Scope 2 GHG emissions and scope covered (see above)

- Indicator 5.3: Volume of counterparty Scope 3 GHG emissions and scope covered (see above). This indicator should be accompanied by details of the calculation methods used and any limitations encountered.

Indicator 5.4: Volume of counterparty Scope 1, Scope 2 and Scope 3 GHG emissions and scope covered (see above).

<u>Articulation with regulations :</u>

The European Regulation of 27 November 2019 on sustainability disclosure in the financial services sector (Sustainable Finance Disclosure Regulation - SFDR) - which started to apply from 2021 - provides that financial market participants - for the investment activities and financial products offered - will have to publish information on the "*Principal Adverse Impacts*" of investment decisions. The Commission published on 6 April 2022 a Delegated Regulation containing the *Regulatory Technical Standards* (RTS) necessary for the implementation of certain provisions. In particular, in Article 5 and its Annex I, the Regulation specifies the information to be provided on the main negative impacts of investment decisions on sustainability factors; this information must include, in particular, the GHG emissions financed by the investments and/or financing provided, i.e. details of the Scope 1, Scope 2 and Scope 3 emissions of the financial actors' counterparties. These provisions will apply from 1 January 2023.

Regarding banking activities, the EBA in its draft technical rules[79] requires large banks to publish information relating to Scope 3 issues of banking activities, with details of their counterparties' Scope 1, Scope 2 and Scope 3 issues. The text provides that information on Scope 1 and Scope 2 issues should be published for the first time by 31/12/2022 (with publication in the early months of 2023). A "phased" approach is foreseen for the publication of Scope 3 emissions: these will have to be published by 30 June 2024 at the latest; during the transitional period, banks will have to explain the methodologies they are developing to measure and estimate the Scope 3 emissions of their counterparties.

[79] "EBA final draft Implementing Technical Standards on Pillar 3 disclosures on ESG risks https://www.eba.europa.eu/eba-publishes-binding-standards-pillar-3-disclosures-esg-risks

The SEC recommendation builds on these various regulatory provisions by asking federations to publish the relevant data on an aggregated basis.

In order to provide this information on their counterparts' emissions, financial actors will depend on the data to be published under the future *Corporate Sustainability Reporting Directive* (CSRD). This directive introduces - for financial and non-financial companies - disclosure requirements on sustainability factors and a requirement for certification by external auditors (the European Financial Reporting Advisory Group (EFRAG) is responsible for specifying the European disclosure standards that will apply). However, this directive should be applicable for the first time as of 1 January 2025 (publication for the financial year 2024) for companies already subject to the "NFRD". In the meantime, financial players will to a large extent therefore have to estimate the amount of these emissions.

Part II: Recommendations on the outcome of the business transformation strategy

The recommendations in this category have two main objectives:

- To make understandable the numerous indicators currently provided, which relate to multiple "green" instruments provided by financial actors without giving information on the share they represent in relation to other financing carried out and in relation to non-sustainable financing;
- To provide an understanding of the dynamics of transformation in the financial sector in relation to the objectives set.

Proposals for the short term

Section 5: Indicator on the amount of funding aligned with the *European taxonomy*

Finding:
The indicators currently provided for the different financial actors are fragmented and not necessarily comparable (green loans, green bonds acquired or structured, green funds, etc.), therefore offering a partial view of investments or financing.

Objectives :
The SEC's recommendation aims to complement the numerous specific indicators currently reported on the OFD with a synthetic indicator, based on a common reference represented by the European taxonomy.

The SEC questioned whether it would be appropriate to recommend that the federations publish information on the setting of quantitative targets by financial players for increasing the proportion of their assets that are aligned with the taxonomy, particularly in the context of determining their alignment strategy. The participants emphasised the premature nature of setting targets, given the recent implementation of the taxonomy, the uncertainty about the stability of its criteria, and the lack of information on the current alignment of their counterparties. It is only after a transition period that the issue of setting targets for progress will really arise.

The SEC also questioned the appropriateness of requiring the publication of the breakdown of indicators for aligning funding with the taxonomy between "sustainable activities", "transition activities" and "enabling activities" (under the current typology of the European taxonomy). Indeed, this distinction still raises key issues and debates, in particular from non-financial companies, which are likely to affect the reliability and interpretation of published information. The SEC prefers to remain consistent with the European regulation that requires the publication of this breakdown - considering that the quality of the information is bound to improve progressively.

Recommendation #6:

The SEC recommends that the federations publish a weighted aggregation of the indicators defined for each category of financial actor by the delegated act adopted pursuant to Article 8 of the Taxonomy Regulation for credit institutions (these indicators are detailed below for credit institutions, portfolio managers, investment firms and insurance undertakings).

The SEC recommends that the breakdown of these indicators into 'sustainable activities', 'transition activities' and 'enabling activities' be published.

Articulation with regulations :
The implementing decree for Article 29 LEC provides for the publication for the investment and portfolio management activities of the relevant actors of :

- The share of "sustainable" stocks, i.e. those that comply with the technical criteria defined by the European taxonomy defining sustainable activities
- The share of exposure to companies active in the fossil fuel sector.

This provision comes into force in 2023 (for the financial year 2022).

The cornerstone of the disclosure requirements is the 2020 Taxonomy Regulation[80] . The delegated act under Article 8[81] sets out in particular the obligations of financial actors:

- Credit institutions must publish primarily a "*Green Asset Ratio*" (GAR), defined as the share of balance sheet assets invested in activities aligned with the taxonomy criteria in the total assets considered. They must provide a breakdown of this GAR into "sustainable activities", "transition activities" and "enabling activities". In addition, credit institutions should publish a similar indicator for assets under management financing activities that meet the taxonomy

80 EU Regulation 2020/852 of 18 June 2020 on a framework for sustainable investment
81 Commission Delegated Regulation 2021/2178 of 6/07/2021 completing Regulation (EU) 2020/852 on taxonomy

criteria and an indicator for fee income from services associated with activities that meet the technical criteria of the taxonomy.

- Portfolio managers must publish a "*Green Investment Ratio*", defined as the proportion of assets under management invested in activities that meet the criteria of the taxonomy.
- Investment firms must publish two indicators, one for their investment service activities and one for services and activities that are not carried out on own account.
- Insurance (and reinsurance) undertakings must publish an indicator relating to their investment activities and an indicator relating to their actual insurance activities (this indicator must be expressed as a share of non-life insurance premiums).

The taxonomy regulation came into force on 1 January 2022 (for the financial year 2021) on a simplified basis (declaration of "eligible" activities in relation to the two climate criteria); full publication (verification of compliance with the two climate criteria) will take place from 1 January 2023 ('financial year 2022') for non-financial companies and from 1 January 2024 ('financial year 2023') for financial companies. The provisions on indicators for banks for their trading book and non-banking services will apply from 1 January 2026 (for reporting in the financial year 2025).

Only financial actors already subject to the NFRD (i.e. listed companies above a threshold of 500 employees) will be subject to the regulation on a mandatory basis. With the entry into force of the CSRD, the threshold for the application of certain requirements is 250 employees. As a result, only certain financial entities will be subject to this disclosure requirement. The others could disclose information on a voluntary basis (notably those that will have to provide information for the preparation of the consolidated statement of their parent company). Federations facing this difficulty will have to be transparent about the representativeness of the information provided (in number and market share).

The SEC's recommendation is that each of the federations should provide aggregated information based on the indicators defined by the taxonomy regulation. It recommends that this be done as early as possible in 2023 before such publication becomes mandatory in 2024.

Section 6: Indicator on investment or financing to large emitting sectors

Finding:
The indicators currently provided do not allow us to judge the importance of funding for "sustainable" activities (in the sense of the taxonomy) compared to funding for "non-sustainable" activities.

Objectives :
The SEC considers it necessary to complement the ratio of taxonomy-aligned funding proposed in the previous recommendation with a ratio to assess the share of 'unsustainable' activities.

In the absence of a consensual definition for these, the SEC recommends retaining the sectors of economic activity that emit the most GHGs. This ratio of "non-sustainable" activities will make it possible to put into perspective the ratio of activities that meet the criteria of the taxonomy.

However, this ratio does not make it possible to distinguish, among the financing granted to the most carbon-intensive activities, between those granted to companies that have not undertaken a transformation towards a carbon-neutral economy and those granted to those engaged in a credible process of decarbonisation of their activities. This distinction is essential in order to assess the real transformation of the activities of financial players: it makes it possible to assess, on the one hand, the financing granted to activities that are already sustainable or to companies that are in a decarbonisation phase and, on the other hand, the financing that is still granted to companies that emit large amounts of GHGs and are likely to continue to do so.

The SEC therefore recommends that the indicator on financing granted to non-sustainable activities be supplemented by an indicator that makes it possible to assess the proportion of this financing that is allocated to companies committed to a credible transition. This information will eventually be obtained through the implementation of the CSRD, which should require non-financial companies to publish a transition plan validated by an external third party (as of 2025 -for the financial year 2024- for non-financial companies and as of this year for those subject to the NFRD). In the meantime, the SEC recommends using information that is already available, i.e. companies with a validated commitment under the SBTi initiative, under ACT[82] or under the Climate Action 100+ initiative (see recommendation 8).

In addition, the SEC recommends calculating an indicator representative of consultancy activities (as defined by Delegated Act 2021/2178 pursuant to Article 8 of the "taxonomy" regulation) for companies in the highest emitting sectors in order to complete the assessment of the share of investments or financing granted alone.

<u>Recommendation #7:</u>

The SEC recommends the creation of two indicators relating to the financing granted to the most emitting sectors:

- Indicator 7.1: Share of financing granted to the most emitting sectors (project financing and corporate financing) in relation to total investments or financing granted. It is recommended to use the

[82] ACT - Assessing Low Carbon Transition - is an international initiative set up in 2018 by ADEME; it aims to provide companies with methodologies to develop strategies and assess the means to achieve the mitigation objective of the Paris Agreement.

nomenclature of sectors "that highly contribute to climate-risks" defined on the basis of the NACE codes adopted by the EBA[83] .

- indicator 7.2: share of funding identified for indicator 7.1 allocated to companies engaged in a transition that has been validated by an external third party (see recommendation 8).

The SEC also recommends calculating an indicator for consultancy activities for companies in the highest emitting sectors:

- Indicator 7.3: Share of net revenue from service activities to the highest emitting sectors in total net revenue from service activities.

The activities covered by this indicator are the same as those covered by Delegated Act 2021/2178 pursuant to Article 8 of the "Taxonomy" Regulation when defining an indicator for service fee income associated with taxonomy-aligned activities.

Articulation with regulations :

In the absence of criteria integrated into the European taxonomy on the harmful impact of economic activities, it is recommended to measure the share of financing granted to the most GHG-emitting sectors (fossil fuels, transport, heavy industry, etc.) based on the nomenclature of sectors "that highly contribute to climate change" defined on the basis of the NACE codes and adopted in particular by the EBA. This text itself refers to "Recital 6 of Commission Delegated Regulation (EU) 2020/1818 supplementing Regulation (EU) 2016/1011 as regards minimum standards for EU Climate Transition Benchmark and EU Paris-Aligned Benchmark", which defines the highly emissive sectors for the European benchmarks, notably the oil, gas, mining and transport sectors.

With regard to indicator 7.2, it will be relevant to use the information published under the CSRD (including transition plans published by non-financial companies - see above) to collect information on non-financial companies engaged in a credible transition.

Section 7: Indicator on funded companies engaged in credible transition

Finding:

There is currently no overall data available within OFD on the financing provided to companies engaged in a credible transition.

However, a measure of the share of financing granted to these companies remains a useful way of assessing the commitment of financial actors to financing the transition.

Objectives :

For this reason, the SEC considers it important that information is provided on the share of all funded companies (whether or not they are high GHG emitters) that are engaged in a credible transition.

[83] "Final draft Implementing Technical Standards on Pilar 3 disclosure on ESG risks "#) January 2022 https://www.eba.europa.eu/eba-publishes-binding-standards-pillar-3-disclosures-esg-risks

The SEC considers it necessary to go beyond the previously recommended indicators (KPI 7.1 and 7.2) focusing on high GHG emitting companies, making a clear distinction between those engaged in a credible transition effort and others. For this reason, it recommends that this information be provided on all funded companies.

Comprehensive and reliable information on the transition engagement of non-financial companies in Europe is currently lacking. The CSRD should fill this gap by requiring non-financial companies to publish their third-party validated transition plan

For the time being, the SEC recommends using the only partial information available, i.e. the voluntary commitment of companies to a process of engagement and validation of their transition objectives. Three initiatives validating the ambition of non-financial companies' commitments have been identified by the CSE:

- Commitments made under the most ambitious '*Science Based Targets*' (net-zero or 1.5°C commitment)[84] .
- Commitments made within the framework of the ACT approach developed by ADEME[85] and recently taken up by the World Benchmarking Alliance[86] .
- Commitments assessed by the Climate Action 100+ Initiative[87] .

The two indicators recommended below offer a partial view of the credibility of the transition, focusing on the non-financial corporate sector, without providing a perspective on other economic sectors (in particular households and sovereign debt instruments). In addition, SMEs and VSEs are often not covered. Therefore, only large companies and a part of the mid-sized companies (MSEs) will be covered[88] .

Recommendation #8:

The SEC recommends calculating several indicators to assess the level of commitment to the transition of funded companies:

- Indicator 8.1: Share of financed non-financial companies with a GHG emission reduction commitment to a third-party validated 1.5°C scenario (SBTi, ACT or Climate Action 100+);

[84] However, it should be noted that SBTi does not verify the level of implementation of these commitments

[85] https://actinitiative.org/fr/

[86] https://www.worldbenchmarkingalliance.org/climate-and-energy-benchmark/

[87] The Climate Action 100+ Net Zero Company Benchmark was launched in March 2021 to assess large companies against the overall objectives of the initiative (emissions reduction, governance, transparency). An assessment of 159 large international companies against the benchmark was published in October 2022. https://www.climateaction100.org/news/climate-action-100-net-zero-company-benchmark-shows-continued-progress-on-net-zero-commitments-is-not-matched-by-development-and-implementation-of-credible-decarbonisation-strategies/

[88] Companies subject to the publication of the Extra-Financial Performance Statement are primarily those listed on a regulated market if their total balance sheet exceeds €20 million or their net turnover exceeds €40 million and if they have more than 500 employees.

- Indicator 8.2: Share of funded non-financial companies with a commitment to an alternative scenario or a commitment not validated by a third party.

Articulation with regulations :

As mentioned earlier, there is currently no regulation to identify non-financial companies engaged in a credible transition. However, this should change with the adoption of the CSRD, which will strengthen the quality of information published by companies in this area (see above)

In the run-up to the implementation of the CSRD, it will be relevant to rely on the transition plans published by non-financial companies to collect information on companies engaged in a credible transition (see above).

Medium-term proposals

In addition to the above recommendations that can be implemented in the short term, the SEC considers it necessary to make a medium-term recommendation (i.e. beyond the next collection of information) setting out a "roadmap" for the various categories of financial actors.

This - more general - recommendation aims to make available information to assess the trajectory of the financial sector towards achieving carbon neutrality by 2050.

Section 8: Developing a sector-specific aggregate measure of portfolio alignment

Finding:

There is currently no information available to assess the dynamics of the financial sector in terms of portfolio alignment in a synthetic way. The previous indicators (indicators 6, 7 and 8) do allow for an assessment of the change in the structure of the investment or loan portfolio (depending on the sector of activity) by providing information on the evolution over time of the respective shares of financing allocated to sustainable activities, to companies committed to a credible transition and to those with high GHG emissions not committed to a credible transition. However, these different indicators do not provide a synthetic assessment.

Objectives :

The SEC believes that it would be useful to provide a summary assessment of the overall transformation of the business of financial actors.

It therefore recommends using a common methodology for measuring alignment within a federation (or even across federations). While the level indicated by each methodology is open to question (as it is highly dependent on the use cases considered and the underlying assumptions), the use of a common methodology over time would allow for an assessment of the alignment dynamics of the sector.

The recommendation aims to encourage players in the same federation to select and use a common alignment methodology, leaving the choice of methodology open. For example, a common measurement of the carbon footprint of financial actors' financing could be envisaged - making it possible to monitor compliance with the reduction commitments made to achieve carbon neutrality by 2050 - or a measurement of the temperature of financing.

Recommendation #9:

The SEC recommends that an aggregate alignment calculation per federation be carried out based on the following steps:

- The choice by each federation of a methodology responding to the recommendations of the SEC of September 2021 on alignment ;

- The calculation by each of the actors of the federations of their level of alignment on the basis of the chosen common methodology;

- The publication of an aggregate alignment indicator of actors within a federation and the distribution of individual indicators.

Section 9: Going Further

The Scientific and Expert Committee also considered whether it would be appropriate to make recommendations on two complementary indicators:

- **An indicator for financing companies in transition**

As an alternative to the indicator proposed in recommendation 8, it would be crucial - for the same reasons - to be able to track financing granted to companies committed to a credible transition regarding the 2050 carbon neutrality objective, in order to differentiate between financing granted to companies that are not committed to a credible transition.

As such, it would be useful to develop an approach to monitor such financing and to replace the indicator proposed in recommendation 8 (based on a proxy). As mentioned above, the use of the information that non-financial companies will have to publish on their transition plan under the CSRD is a particularly interesting avenue to explore. However, it will be necessary to ensure that the requirements of the CSRD regarding the reference scenario are met, as well as the quality of the external validation required by the regulations.

- **An indicator on the quality of transition plans of financial actors**

The above indicators are intended to give an overall view of the financing granted in favour of the transition. These indicators could be usefully complemented by an indicator on the quality of the transition plans adopted by the financial actors themselves with a view to achieving carbon neutrality by 2050. This indicator would make it possible to assess the momentum of financial actors to achieve carbon neutrality through an indicator of the quality of transition plans published under the CSRD.

Despite the paramount importance of these issues, the SEC preferred to postpone the publication of recommendations on these various indicators pending both a better visibility of regulatory developments and the completion of work undertaken at the international level (notably within the G20 Sustainable Finance Working Group, the Financial Stability Board and the NGFS (*Network For Greening the Financial System) in* order to assess the relevance of net-zero commitments and the quality of transition plans.

VI. Declaration of intent on fossil fuels

In February 2021, the SEC published recommendations on indicators for financing and investment in the coal industry and, in September 2021, on those for unconventional hydrocarbons. These recommendations are still relevant, although at this stage they only cover a partial view of financial market activity (they are more focused on the activity of banks). The minimal agreement reached at COP 27 on the exit from fossil fuels, the energy and macro-financial context, as well as the current organisation of the indicators and data actually published on the OFD, justify their content and scope.

Firstly, the SEC noted once more the urgency of the IPCC's 6th Assessment Report (2021-2022), which highlights :

(i) the likely overshooting of the Paris Agreement temperature thresholds during the 21st century in the absence of deep cuts in greenhouse gas emissions - and the inexorable biophysical and human societal effects of such warming;

(ii) the finding that the cumulative greenhouse gas emissions projected for the lifetime of existing and currently planned fossil fuel infrastructure (without mitigation measures) exceed the cumulative net greenhouse gas emissions of the 1.5°C no-overshoot or limited-overshoot and 2°C high-confidence warming trajectories;

(iii) the need for rapid, deep and, in most situations, immediate reductions in greenhouse gas emissions across all sectors, including *through* a shift from fossil fuels (without capture and storage technologies) to low or zero carbon energy sources.

These findings were reiterated by the International Energy Agency, both in its May 2021 "net-zero" scenario (*i.e.*, no more new oil and gas fields, coal mines and power plants) and in its November 2022 "net-zero" transition report on coal (*i.e*, reduction in coal use of around 90% by 2050 and full decarbonisation of the global power generation sector by 2040, in a context where emissions from existing coal assets lead to the 1.5°C threshold being exceeded.

However, the SEC notes the increasing consumption of fossil fuels worldwide, the significant increase in financing for fossil fuels (including their development), limited investment by oil and gas companies in the development of carbon-neutral or low-carbon energy infrastructure, and increasing risks to financial stability.

Recent reports by the International Energy Agency (World Energy Outlook, November 2022; World Energy Investment Report, June 2022) and the International Monetary Fund's *Global Financial Stability Report* (October 2022) have highlighted stark findings on the need for a rapid alignment of capital flows to the carbon neutral transition:

(i) a net recovery in investment in coal and oil/gas infrastructure since the Covid-19 pandemic (*e.g.* USD 380 billion in oil and gas in 2021, before the start of the war in Ukraine, compared to ~USD 16 billion in low-carbon fuels; ~USD 800 billion of debt stock in coal development in emerging and developing economies in summer 2022, about 4 times as much as in the aftermath of the Paris Agreement in January 2016) ;

(ii) limited investment by oil and gas companies in the development of renewable infrastructure, of the order of 5% of Capex in 2022 (although this amount has doubled since 2020, and European companies have made up the bulk of this investment);

(iii) despite the focus of banking institutions (mainly) on the transition (or divestment) of coal, Arctic and oil sands assets, the academic literature shows that returns on new bonds issued by fossil fuel companies have been more responsive to climate policies than returns on syndicated bank loans, demonstrating that banks are not yet pricing the risk of stranded assets to the same extent as bond markets. This is in addition to the assessment of the significant exposure of European market participants to the development of new fossil fuel infrastructure around the world, in particular *through* debt issuance.

For all these reasons, the SEC is working on both the reorganisation and the substantial strengthening of the fossil fuel indicators, with particular attention to the full coverage of market players and geographical exposures, the challenges of developing new infrastructure, and those related to the transition of the oil and gas industry (still limited, including in Europe).

At this stage, the SEC has chosen to focus on two elements: (i) the assessment of the weakness of the existing OFD, in terms of indicators and published data; and (ii) the elaboration of recommendations aimed at updating and consolidating the indicators, both on coal and on the oil and gas industry.

Regarding coal, the continuing significant increase in financing in the coal industry, and the associated transitional issues, oblige the SEC both to strengthen these indicators and to reiterate the fundamental importance - including for those players in the Paris financial centre whose exposure remains significant (although decreasing) - of displaying them in their entirety, and demonstrating methodological robustness.

Regarding oil and gas, the SEC recognises the *de facto* limited scope of the September 2021 recommendations on unconventional hydrocarbons - which nevertheless had the important merit of highlighting the levels of exposure of the Paris financial centre to oil and gas, as well as the complex transition issues of this industry. However, meeting the temperature targets of the Paris Agreement implies a profound decarbonisation of the sector in its entirety - in a difficult energy, geopolitical and macro-financial context that is prone to delaying the objectives of financing the transition.

In this context, and given the lesser attention paid to the oil and gas industry in the discussions and initiatives of the Paris financial centre at this stage, it appears that the information published on flows and exposures is largely incomplete, when informed.

It is therefore essential, both because of the current context and in order to affirm the credibility of the process of decarbonisation of the French economy, that the SEC deepen its recommendations on all of these energies, with a view to comprehensive, robust and useful publications on the OFD in 2023.

In its next publication, due out in the first quarter of 2023, the SEC intends to further develop its recommendations to the federations on :

- The cross-sectional information published on the coal industry; the scope covered by the indicators within the coal institution as well as the diversity of financial market players active in this sector (and its expansion);
- Indicators of the amount of exposure to the oil and gas industry as a whole, by type of asset ;
- Indicators relating to the levers and modalities of action of market players in the transition of the coal and oil industries, respectively; and
- Indicators on the incentives for the development and implementation of exit plans within the coal industry provided by market players, as part of the commitment on coal assets in stock, but also - and more importantly - by the oil and gas industry as a whole.

The SEC will ensure that it publishes recommendations on aggregate indicators, as well as providing microeconomic visibility on the exposure and incentives for transition provided by market players, according to the type of business and the different associated policy levers.

VII. Presentation of the Scientific and Expert Committee

The Committee is composed of a chairman, a secretary and several colleges: two members from NGOs or think tanks, four academic members, two members representing public authorities, and two experts with knowledge of the banking and investment business.

Members are appointed "intuitu personae" by the Finance ClimAct Steering Committee. They therefore speak in their own name and not on behalf of their institutions, with the exception of the representatives of DG Treasury and MTECT, although they bring the expertise and knowledge of their respective organisations. They may also play a reporting and communication role internally within their respective organisations.

The Secretary of the SEC assists the Chairman and ensures the smooth running of the Committee.

President : Pierre-Louis Lions - Fields Medal winner in 1994, Professor at the Collège de France, President of the International Scientific Committee of the Louis Bachelier Institute and of the Green & Sustainable Finance Transversal Program.

Secretary: Stéphane Voisin

NGO and Think Tank Members:

Lucie Pinson

Michel Cardona

Academic Members :

Anna Creti

Delphine Lautier

Augustin Landier

Peter Tankov

Emmanuel Hache

Expert Members:

Jérôme Courcier

Guillaume Neveu

Charlottes Gardes-Landolfini

Public Members:

Julie Hanot and Aurélien Girault - Ministère de la Transition écologique et de la cohésion des territoires

Benjamin Dartevelle – DG Trésor