

Faculty of Law, Economics and  
Finance of the University of  
Luxembourg

## THE EU GREEN DEAL & THE NEW EU SF AGENDA

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UNIVERSITÉ DU  
LUXEMBOURG





LE GOUVERNEMENT  
DU GRAND-DUCHÉ DE LUXEMBOURG  
Ministère des Affaires étrangères  
et européennes



FACULTY OF  
ECONOMICS  
AND FINANCE

« A Luxembourg-based academic research think-tank, united with focused researchers across the Globe in the effort to understand the impact of ESG challenges on the planet and society and how best to address them with legal and non-legal means, with a view to mitigating their adverse effects on mankind. »

- Three departments
- More than 100 researchers
  - International network
- Global and regional impact

- The **FDEF Centre for Sustainable Governance and Markets** (CSGM) functions as virtual research platform for the sustainability expertise of three departments, four academic disciplines, over 200 researchers and 18 nationalities cooperating in the Faculty of Law, Economics and Finance at the University of Luxembourg.
- The CSGM bundles sustainability research with a special view to sustainable governance and markets – ranging from the institutional, legal and economic ordering over the impact analysis of a changing environment to social effects.
- Sustainability, as understood by the CSGM, relates to the European Commission's Green Deal as well as the United Nation's seventeen [Sustainable Development Goals](#) – the United Nation's blueprint to achieve a better and more sustainable future. The UNSDGs address the global challenges, including those related to climate change, poverty, gender, inequality, exclusion, environmental degradation, migration, peace and justice.

**1.**

**BUSINESS &  
HUMAN RIGHTS**

**2.**

**DEVELOPMENT  
ECONOMICS &  
DEVELOPMENT  
FINANCE**

**3.**

**FINANCIAL  
INCLUSION**

**4.**

**FINANCING THE  
FIGHT AGAINST  
CLIMATE CHANGE**

**5.**

**CLEAN ENERGY &  
CLIMATE-NEUTRAL  
ECONOMY**

**6.**

**GENDER,  
INEQUALITY  
AND CONFLICTS**

**7.**

**GREEN  
SUPPLY CHAINS**

**8.**

**GREEN  
ACCOUNTING**

**9.**

**MIGRATION**

**10.**

**RULE OF LAW  
& DEVELOPMENT  
COOPERATION**

**11.**

**SUSTAINABLE  
GOVERNANCE  
STRUCTURES  
IN EUROPE**

**12.**

**SUSTAINABLE  
FINANCE**

I. A Look Back – the SFAP of 2018

II. Green Deal – what is in for SF?

III. The renewed SF Agenda – What is to come?

IV. Critique & Comments

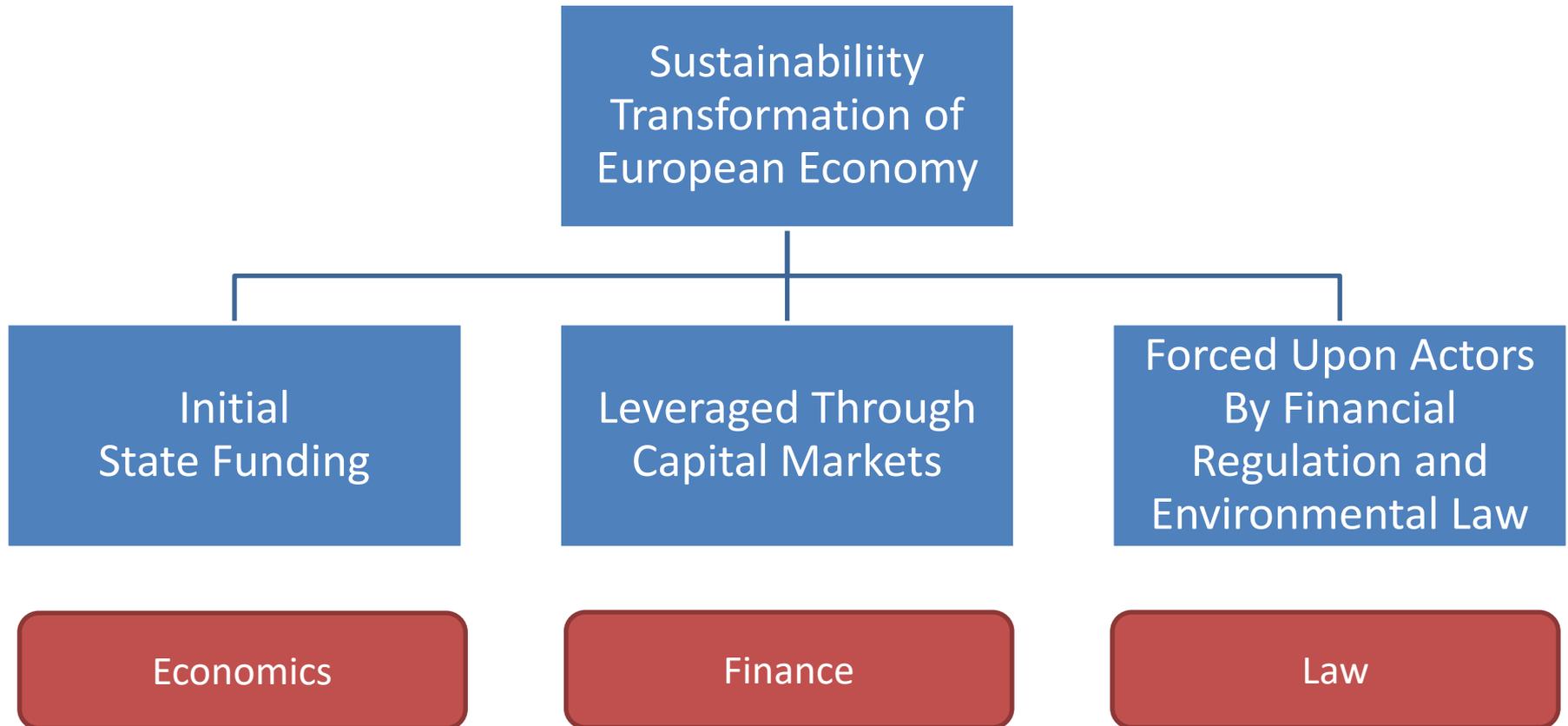
V. Conclusion

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# I. SFAP 2018

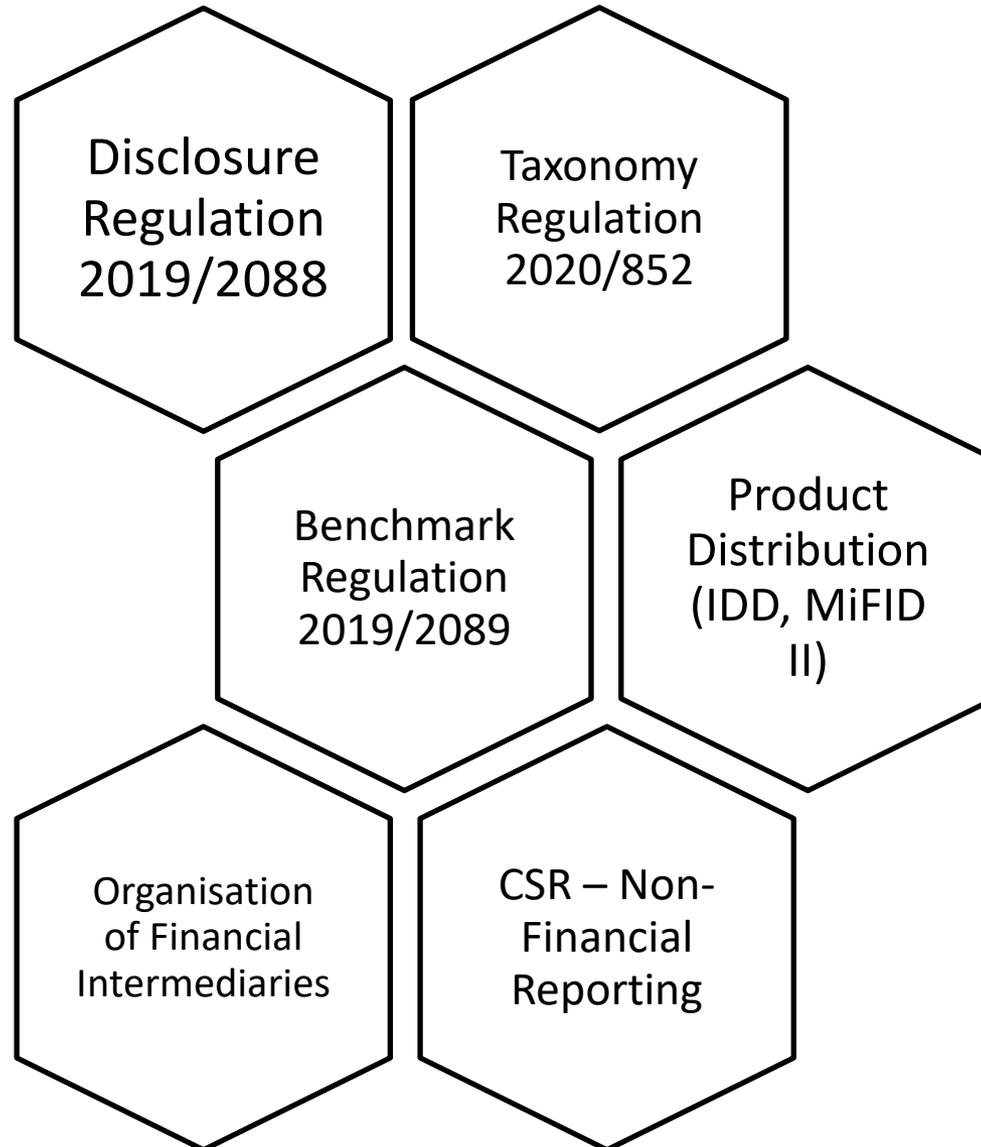
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# The Concept of the EU Sustainable Finance Action Plan



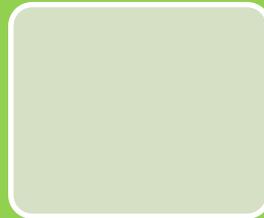
# SFAP 2018 – six core initiatives

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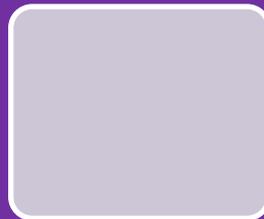




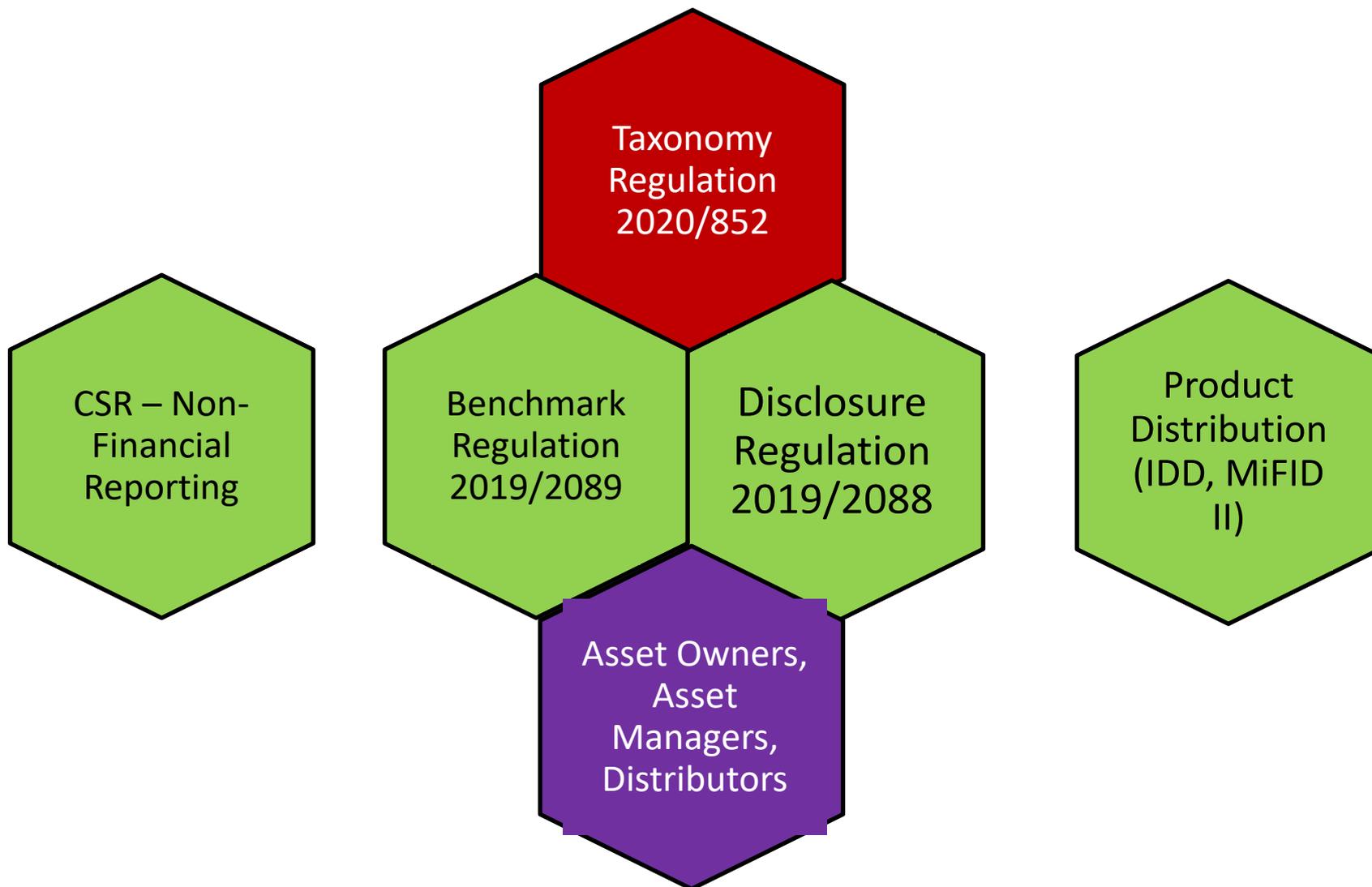
What is sustainable? (terminology)



Who is sustainable?



Acting sustainably



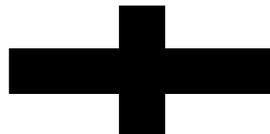
# Sustainability as defined by the European Commission (Art 3 of the EU Sustainability Taxonomy Regulation)

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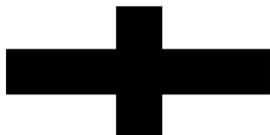
Substantial contribution to one environmental objectives (e. carbon neutrality, biodiversity etc. - all defined by the Taxonomy Regulation)

Prof. Hoepner's presentation



Economics

Does not significant harm (DNSH) to other environmental objectives



Law

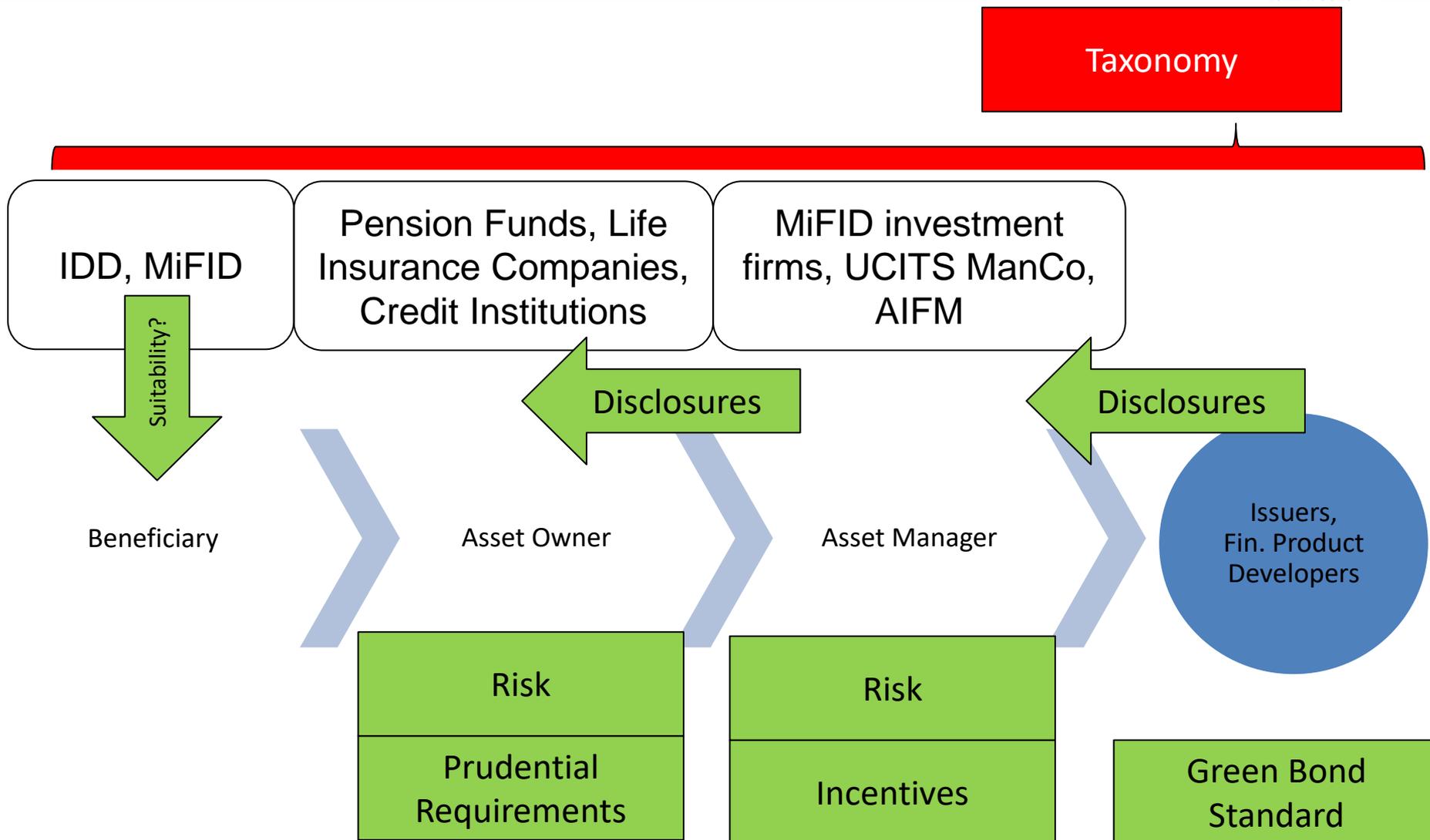
Compliance with Minimum Legal Safeguards (Art. 18 Taxonomy Regulation)

OECD Guidelines for  
Multinational Enterprises  
(supply chain, liability etc.)

UN Principles for  
Business and Human  
Rights

UN&ILO Minimum Labour  
Laws, work safety, Social  
Insurance

# Disclosure Requirements across the FS Value Chain



- Distribution: integrate ESG into « suitability test » on behalf of clients
- Organisation: remuneration?
- Operations: consider ESG risks in daily operations; adjust fiduciary duties (not: always invest sustainable!)
- Risk Management: Consider (very) long-term impact
- « Suitability » for distribution, investments?



Asset Owners,  
Asset  
Managers,  
Distributors

# Potential Impact of SFAP

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- Clarifying terminology
- Ensuring comparability
- Rendering sustainable finance the new normal
- Questions marks on organization (to be continued)

⇒ *Nudging* towards sustainability

⇒ Not: mandating sustainability

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## II. Green Deal – what's in for SF?

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# The EU's New Green Deal

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- (even) more capital
- Public-private partnerships
- Additional EU programmes
- From high to super-high on the agenda
- Enhanced speed
- New Sustainable Finance Agenda – consultation March 2020 onwards

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## III. Renewed SF Agenda

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# 1. Renewed SF Agenda consultation

- 1. Strengthening the foundations for sustainable investment by creating an enabling framework, with appropriate tools and structures.** “Many financial and non-financial companies still focus excessively on short-term financial performance instead of their longterm development and sustainability-related challenges and opportunities.”
- 2. Increased opportunities to have a positive impact on sustainability for citizens, financial institutions and corporates.** “This second pillar aims at maximising the impact of the frameworks and tools in our arsenal in order to “finance green”.”
- 3. Climate and environmental risks will need to be fully managed and integrated into financial institutions and the financial system as a whole, while ensuring social risks are duly taken into account where relevant.** “Reducing the exposure to climate and environmental risks will further contribute to “greening finance”. Objectives of this consultation and links with other consultation activities.”

# 1. Renewed SF Agenda consultation

- Furthering green funds?
- asking retail investors about preferences?
- consumers' financial literacy
- Measures against short-termism?
- passive index investing
- adapting rules on fiduciary duties, best interests of investors/the prudent person rule, risk management and internal structures and processes in sectorial rules **to directly require them to consider and integrate adverse impacts of investment decisions** on sustainability (negative externalities)

⇒ From nudging to mandatory?

## 2. Consultation on L2 measures re the asset man't sector – closed 7/2020

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- ESA statement of July 2020 [...]

### 3. AIFMD II review – consultation of 23 Oct 2020

- KPMG report more or less silent on SF
- COM AIFMD II review: considering renewed SF agenda
- **AIFMR Regulatory Reporting template (62.1):**  
If more detailed portfolio reporting? more details on sustainability-related information, e.g. risk exposure and/or impacts? E.g. sustainability-related data, in particular on exposure to climate and environmental risks, including physical and transition risks (e.g. shares of assets for which sustainability risks are assessed; types and magnitudes of risks; forward-looking, scenario-based data)

### 3. AIFMD II review – consultation of 23 Oct 2020

- Full section on ESG/ sustainability (p. 77 et seq.)
  - Question 91. Should **investment decision processes** of any AIFM **integrate the assessment of non-financial materiality**, i.e. potential principal adverse sustainability impacts?
  - Question 92. Should the adverse impacts on sustainability factors be integrated in the **quantification of sustainability risks** (see the example in the introduction)?
  - Question 93. Should AIFMs, when considering investment decisions, be required to take **account of sustainability-related impacts beyond what is currently required by the EU law** (such as environmental pollution and degradation, climate change, social impacts, human rights violations) alongside the interests and preferences of investors?

### 3. AIFMD II review – consultation of 23 Oct 2020

- Full section on ESG/ sustainability (p. 77 et seq.)
  - Question 94. The EU Taxonomy Regulation 2020/852 provides a framework for identifying economic activities that are in fact sustainable in order to establish a common understanding for market participants and prevent green-washing. To qualify as sustainable, an activity needs to make a substantial contribution to one of six environmental objectives, do no significant harm to any of the other five, and meet certain social minimum standards. **In your view, should the EU Taxonomy play a role when AIFMs are making investment decisions, in particular regarding sustainability factors?**
  - Question 95. Should other sustainability-related requirements or international principles beyond those laid down in Regulation (EU) 2020/852 be considered by AIFMs **when making investment decisions?**

⇒ From nudging to mandatory?

## 4. Main takeaways from 10+ ESMA statements

- General concerns about the lack of a “clear and appropriate taxonomy and labels” on ESG terms **at the time investment firms, institutional investors and assets managers are requested to disclose** how they integrate sustainability risks in the investment decision-making process or advisory process
- **importance of proportionality** to allow a smooth sustainability transition to smaller firms
- Adoption of a **principle-based approach.**

⇒ A message of caution

## 4. Main takeaways from 10+ ESMA statements

- Data is key => **single EU data platform covering both financial and ESG information**
- Sound risk management
- Ensure investors and consumers have access to SF products safely and transparently
- Supervisory convergence

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## IV. Comments & Critique

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# 1. DATA

- Right now we do not know how sustainability impacts on profitability
  - Data missing, incomplete
  - Regulators flying blind
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- Frankfurt School UCITS study (2020): 28 out of 101 « green » UCITS did not disclose sufficient data; cash flows of the remainder often currently not uniformly classified by taxonomy
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- ⇒ Not even speak about traditional UCITS
  - ⇒ Further work necessary
  - ⇒ Standing the test of reality

## 2. Transformation

- UCITS study: only 3 out 101 « green » UCITS qualify as green under Taxonomy
- Huge portfolio reallocation required
- New generation of technological and economic models
- Model risk, tech risk
- Economic impact?

# 3. Risk management

- Risk management data trail missing
- Risk models require adjustments.
- Data providers not up to date.
- Backward testing non-existent, deficient.
- Taxonomy effect needs to be absorbed.

## 4. Remuneration models

- Drafting sound remuneration schemes is a (legal) challenge already in the absence of sustainability
- Does not become easier with sustainability due to a lack of historical data, lack of experience.
- Unwanted effects / perverse incentives

# 5. Prudential rules

- Ensure enhanced model building with regard to SF data
  - Refine existing models (ask intermediaries to self-develop!)
  - BUT: risk of error enormous; soft approaches > hard approaches
- ⇒ Avoid detailed CRR style rules across the FS sector
- ⇒ Code-style / comply or explain approaches / open standards > rules

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## V. Conclusion & Thesis

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- Sustainable Finance is of paramount importance.
- Taxonomy aims at same language, disclosure at data. Good.
- **Sound regulation** on the organization of intermediary requires data and prudent assessment of risks and unwanted effects of regulation; regulators fly in the dark.
- Nudging approach of SFAP I ambitious, not yet absorbed. Mandatory SF investments not advisable with current lack of data.
- Wanting too much in too short of time often prompts unwanted effects.

# Conclusion – the right regulatory order

Step 1: Implement taxonomy across sectors

Step 2: Ensure reporting based on taxonomy ;

Step 3: Collect data (and ensure data platforms, comparability etc.)

Step 4: Assess data with some representative time series

Step 5: draft rules & standards on the organization of intermediaries

Step 6: review whether shift from nudging to mandatory > costs.

# Thank you!



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