Written Evidence submitted by WWF-UK to the Financial Services and Markets Bill Commons General Committee (FSMB19)

INTRODUCTION

1. WWF is the world's leading independent conservation organisation. Our mission is to create a world where people and wildlife can thrive together. WWF welcomed the government's COP26 commitment that the UK will become the world's first net zero financial centre, the recent launch of the Transition Plan Taskforce and the formation of the Glasgow Financial Alliance for Net Zero (GFANZ). We believe the power of the financial system must be harnessed to drive net zero and nature commitments. In this regard we help develop science-based guidance and policy recommendations to ultimately move closer to a net zero, nature-positive global financial system and economy.

2. At WWF-UK, we have deep expertise in green finance and financial regulation. Our team comprises individuals with experience and expertise from working in both large and small financial institutions in the UK and abroad, and from working directly on financial sector regulation in the public sector in the UK. Additionally, WWF-International hosts a multinational 'finance practice', pooling financial expertise from across all of WWF's national offices. More recently, WWF have been well represented within the Transition Plan Taskforce, including leading a workstream of work on the inclusion of nature in transition plans. As such, we welcome the opportunity to contribute to this call for written evidence and hope to have the opportunity to provide oral evidence to the committee, to inform its work and the Bill's development in general.

SUMMARY

3. The UK's departure from the European Union (EU) has necessitated significant changes to the way in which financial services policy is made in the UK, and to how the UK regulates the industry. WWF-UK acknowledges the complexity and breadth of these changes and welcomes the government's efforts in this Bill to provide a clear, coherent framework for financial services in future.
4. Our primary concern with this Bill is its failure to take into account the importance of financial services in progressing towards achieving the UK's net zero, climate and nature goals, including the government's commitment to making the UK the world's first net zero financial centre. This Bill presents a "once in a generation opportunity" to ensure that issues of climate and nature are properly accounted for in financial regulation. However, it currently fails to provide a sufficient legal basis for future financial regulation to be aligned with the government's existing commitments and thereby seize on the enormous opportunity for people, businesses and the government that the green finance transition presents.

The Future Regulatory Framework ('FRF')

5. The FRF offers a crucial opportunity for the UK to fulfil its potential to lead the global transition to green finance. We will only have a financial system that aligns with net zero and supports a booming green finance sector if financial institutions, the real economy, government and regulators are all pulling in the same direction. An appropriate regulatory framework, with appropriate objectives, is required.
6. The government must ensure that its regulatory approach in future meets its ambitions in this area. The Bill currently fails to sufficiently incorporate climate and nature goals as part of the UK's future regulatory framework.
7. That is why WWF, alongside other NGOs and the private sector have been calling for a climate and nature secondary statutory objective as part of this new framework.

Key Bill ask 1: Statutory objective for the financial regulators on climate and nature.

Other issues

8. Transition plans: Net zero transition plans should be mandated in this Bill, and the government or regulators should be given powers to require specified companies and institutions to detail how they plan to reach net zero by 2050 and nature positivity by 2030 in the short- and medium-term.

Key Bill ask 2: Mandatory transition plans.

9. Sustainability Disclosure Requirements (SDRs): It is unclear when and how SDRs will be brought in in future. To provide business certainty, we urge the government to provide clarity on the status of the SDRs, and to legislate for them through this Bill.

Key Bill ask 3: The implementation of SDRs.

WWF RESPONSE

Future Regulatory Framework

The problem

10. The government's Future Regulatory Framework (FRF), delivered through this Bill, will determine how financial services regulation is developed in the UK in future. The proposals include a major delegation of powers to, and renewed objectives for, the regulators.
11. The regulatory objectives and principles that Parliament sets within the new regulatory architecture are therefore critical. They will determine all future rules that structure and support the UK financial services industry. This makes the FSM Bill a unique legislative moment for both climate action and nature protection and the key moment to ensure that the UK's commitment to building a net zero financial centre is delivered.
12. Almost two years ago, the Committee on Climate Change made clear that climate risk and net-zero must be fully integrated into financial regulation for the UK to achieve

its legally binding net zero target under Section 1 of the Climate Change Act 2008. This Bill is the obvious vehicle for delivering this.

13. Without acting now to strengthen the rules being developed for the financial sector, the government will not realise its own ambitions to build a net zero financial sector, or meet its own legal obligations, as per a high court judgment earlier this year, ordering the government to outline exactly how its net zero policies will achieve emissions targets.

14. Fifteen years ago, Sir Nicholas Stern described climate change as the biggest market failure we've ever seen where the costs on society of environmentally harmful activities haven't been internalised. This market dysfunction contradicts the existing regulatory objective of relevant markets functioning well and market integrity. In the long run, the dire risks of not meeting our net zero goals will dwarf any short-term economic and financial gains in economic competitiveness, as per reports from the International Monetary Fund and World Economic Forum.

15. It is also critical to recognise that net zero and nature are deeply interconnected issues that must be tackled together. This Bill is key to tackling nature destruction and commitments under the G7 2030 Nature Compact and G7 Leaders Pledge for Nature, for instance.

16. Moreover, all Intergovernmental Panel on Climate Change scenarios that keep us within 1.5°C require the halting and reversing of nature loss.

17. Put simply, we need a nature positive economy to achieve our net zero goals, and we need that reflected in the activity of financial markets. The importance of climate and nature to the future of the UK economy is now well documented, for example through the Dasgupta Review on the Economics of Biodiversity. WWF'-UK's response can be found here.

18. Therefore, the UK's financial regulators must have a climate and nature objective, giving them a clear legal mandate to take appropriate action.

The status quo

19. Currently, the Bill amends one of eight existing 'regulatory principles' for the FCA and PRA, so that instead of acknowledging the desirability of sustainable growth in the UK, the regulators would take into account "the need to contribute towards achieving compliance with section 1 of the Climate Change Act 2008 (UK net zero emissions target)."

20. Independent legal analysis confirms that this regulatory principle would not provide a sufficient basis for the regulators to act to facilitate the transition to a net zero-aligned financial centre. To discharge this duty, regulators would only have to consider it – but could depart from it.

21. This crucial point was underlined recently when the PRA stated that they "do…not have an explicit ESG remit". Moreover, as stated in the government's FRF consultation, "the regulators are not required to act to advance their regulatory principles; instead they must take them into account when pursuing their statutory objectives."

22. Furthermore, the current drafting of the principle itself is weak – requiring the regulators to have regard to "the need to contribute towards" achieving compliance

with the net zero target. In practical terms, this means that the regulators would need to do very little (or virtually nothing) to discharge this duty.

23. As currently drafted, the FSM Bill would also require the regulators to act to further competitiveness and growth, over and above action to promote a net zero aligned economy, likely hindering the ability of the UK to meet its legally binding net zero and broader environmental targets and the rapid achievement of a world leading net zero-aligned financial centre.
24. A new climate and nature objective would also directly contribute towards the FCA's operational objective of protecting and enhancing the integrity of the UK financial system (in a way that, for example, the proposal on competitiveness and growth, does not).

The solution

25. A statutory objective on climate and nature, on the other hand, would compel regulators to play the essential, proactive role required of them in facilitating the green finance and economic transition. The regulators would have to actively advance alignment of the finance sector (and UK economy as a whole) with climate and nature targets in their policies, rulemaking, guidance and supervision.
26. With this amendment, the FCA could, for example, ensure that firms make credible claims about environmental performance, standardise the use of metrics across the market and provide guidance on adaptation finance, or ensure that the UK's finance sector does not contribute towards deforestation.
27. A secondary statutory objective would also provide a stronger mechanism to hold organisations to account for actions which hinder (rather than facilitate) the necessary transition to net zero.
28. In hierarchical terms, secondary objectives do not interfere with achieving primary objectives. A secondary statutory objective would still sit underneath the primary strategic objective for the regulators and the operational objectives for the FCA.
29. The Social Market Foundation and others have analysed the potential exports and jobs opportunities that could arise from the UK capitalising on its comparative advantage in green financial services. The net zero/nature objective will ensure that growth and competitiveness is aligned with the long-term goal of achieving a net zero financial sector.
30. The additional steps that HMT has legislated for, such as statutory panels, rule reviews and cost-benefit analysis frameworks, should also provide ample opportunity for any unintended consequences to be identified and mitigated prior to any rules coming into effect.

Other jurisdictions

31. Moreover, other regulators around the world already have statutory objectives on climate and broader environmental issues.

32. The German regulator has a sustainability objective which integrates sustainability issues into its supervisory activities, with a focus on combatting "greenwashing."

33. The French regulator must oversee the quality of information provided by asset managers in relation to their investment strategies and their management of risks linked to the effects of climate change, under Article L621-1 of the Code monétaire et financier). With this objective, it has set up the Climate and Sustainable Finance Commission and has committed to sustainable finance by 'changing practices, increasing transparency and facilitating the consideration of sustainability issues and the mobilisation of capital for more sustainable activities'.

34. Since 2019, the French regulator has had a mechanism for monitoring and assessing the climate-related commitments of Paris financial centre institutions and it publishes an annual report on these commitments and how they will actually be implemented.

35. These countries recognise that climate and nature are integral to the proper functioning of the financial system. The UK must also recognise this and ensure that climate and nature are properly embedded in the Future Regulatory Framework, to achieve a world leading green finance sector. As things currently stand, the UK is falling behind its international competitors.

How this would work in practice

36. There are several practical examples where this would be of benefit too, such as with:

- The Prospectus Regulation;
- The Markets in Financial Instruments Directive II (MiFID II);
- The Alternative Investment Fund Managers Regulation (AIFMD), and;
- The Undertaking for Collective Investment in Transferable Securities Directive (UCITS).

37. For illustrative purposes, below is an explanation of how a new objective would work in practice with relation to prospectus reform.

Case Study: The Prospectus Regulation

- The government recently reformed the EU's Prospectus Regulation to streamline the process of producing prospectuses for both listed and unlisted companies offering securities to the public.
- The government plans to provide the FCA with the ability to determine when prospectuses are required, and what content requirements might be.
- The government has been keen to encourage more forward-looking information in prospectuses in future, to help investors decide where to invest.
- As currently drafted, the FSM Bill would not require the regulators to make rules requiring firms to provide information on the likely environmental impact of their operations in future.
- With a secondary objective on climate and nature, regulators would almost certainly do so – ensuring that investors are fully conscious of the environmental impacts of their investments.

The business opportunity

38. In a challenging economic climate, the green transition also offers an enormous opportunity for people and businesses, and for the government to deliver a net-zero financial centre, as promised at COP26. A recent study by WWF and Scottish Power found that green upgrades could cut UK energy bills by £1,800 a year. Supplying the goods and services to enable the global net-zero transition could be worth £1 trillion to UK businesses by 2030.
39. The Government positioned the UK to capitalise on this business opportunity by committing to reaching net zero by 2050 and hosting the world's first net zero financial centre. Low-carbon financial services could generate an export opportunity of up to £7.5bn per year in 2030, rising to £17bn per year by 2050. However, the UK won't lead the global green finance sector without the right regulatory framework to support it.
40. A new objective for the regulators would ensure that the UK has a booming green finance sector, which requires: a transparent and trusted market; certainty about the direction of climate related disclosures and unequivocal system-wide alignment; world leading standards and influencing those internationally.
41. A new objective would also provide the financial sector with certainty about the regulatory direction of travel on net zero, benefitting the sector and wider economy through the transition. This is something that businesses repeatedly ask for, and we understand that leading financial institutions will be writing to the committee in relation to this.

Other issues

Transition plans

42. At COP26 last year, the Chancellor committed to requiring asset managers, regulated asset owners and listed companies to publish transition plans that consider the government's net zero commitment (or provide an explanation as to why one has not been produced). The Treasury announced that they intend to legislate to deliver on this commitment. This is because net zero transition planning is a critical component of the UK's pathway to achieving its net zero and international objectives.
43. Several other international bodies have also developed work around transition planning.
44. The International Financial Reporting Standards Foundation (IFRS) have set out requirements for identifying, measuring and disclosing climate-related risks and opportunities. The Glasgow Financial Alliance for Net Zero convenes over 500 financial institutions globally to develop recommendations and guidance for credible net zero transition plans. Meanwhile, the European Financial Reporting Advisory Group have developed their own disclosure requirements.
45. This Bill is the obvious and critical opportunity with which to legislate for transition plans; they are well within scope as they should be considered a fundamental aspect of the UK's new vision for financial services.

46. The Transition Plan Taskforce (TPT), which aims to develop a gold standard for climate transition plans, has subsequently been working to develop guidance and best practice to drive high quality net zero planning for FS companies and corporates and help avoid greenwashing. WWF has representation in multiple levels of the TPT and has been asked to lead a workstream on the inclusion of nature in transition plans.

47. However, there is currently a disconnect between this work and current legislation, as this Bill does not legislate for transition plans and therefore the relevant organisations above are currently not obliged to produce them.

48. This is despite the lack of data, transparency, standardisation and comparability between companies' ESG and sustainability objectives being the most commonly cited set of barriers to financiers in their allocation of green capital – see page 21 of the Advisory Group on Finance for the Climate Change Committee's report on net zero finance. This barrier is being addressed by the standards being developed by the TPT.

49. A continued reliance on voluntary disclosures is insufficient and will not ensure that net zero is reached in time. This is explained further on page 22 of WWF-UK's review of FTSE-100 net zero commitments.

50. Regulation underpinning such standards ensures credibility and trust and protects investors against reputational and credit risks associated with greenwashing.

51. To further support the effective development of a world-leading green finance sector in the UK, this Bill should therefore oblige organisations to produce transition plans.

52. If it does not, the UK risks falling behind its competitors, including the EU's Corporate Sustainability Reporting Directive (CSRD) and Corporate Sustainability Due Diligence Directive (CSDDD).

53. A failure to legislate will also lead to a continued delay of the necessary data needed by market participants to manage risks related to climate change and protect consumers. It will lead to continued uncertainty for institutions as to what their plans should look like, who will enforce them, how they will be held to account if they do not meet the required standards, and when legislation will be forthcoming.

Sustainability Disclosure Requirements (SDRs)

54. In July 2021 the government announced new Sustainability Disclosure Requirements, designed to bring together existing sustainability-related disclosure requirements under one cohesive framework.

55. It is currently unclear why this has not been included in the Bill, or when and how these requirements will be brought in in future.

56. If the government fails to include these requirements in legislation, this will severely reduce private sector confidence in the government's position. The global race for primacy, as per the work happening internationally mentioned above, is already underway, and the UK would risk falling behind.

57. This Bill should implement these requirements in legislation and create a clear legal framework for information flows between corporates and investors.

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