KING'S College LONDON

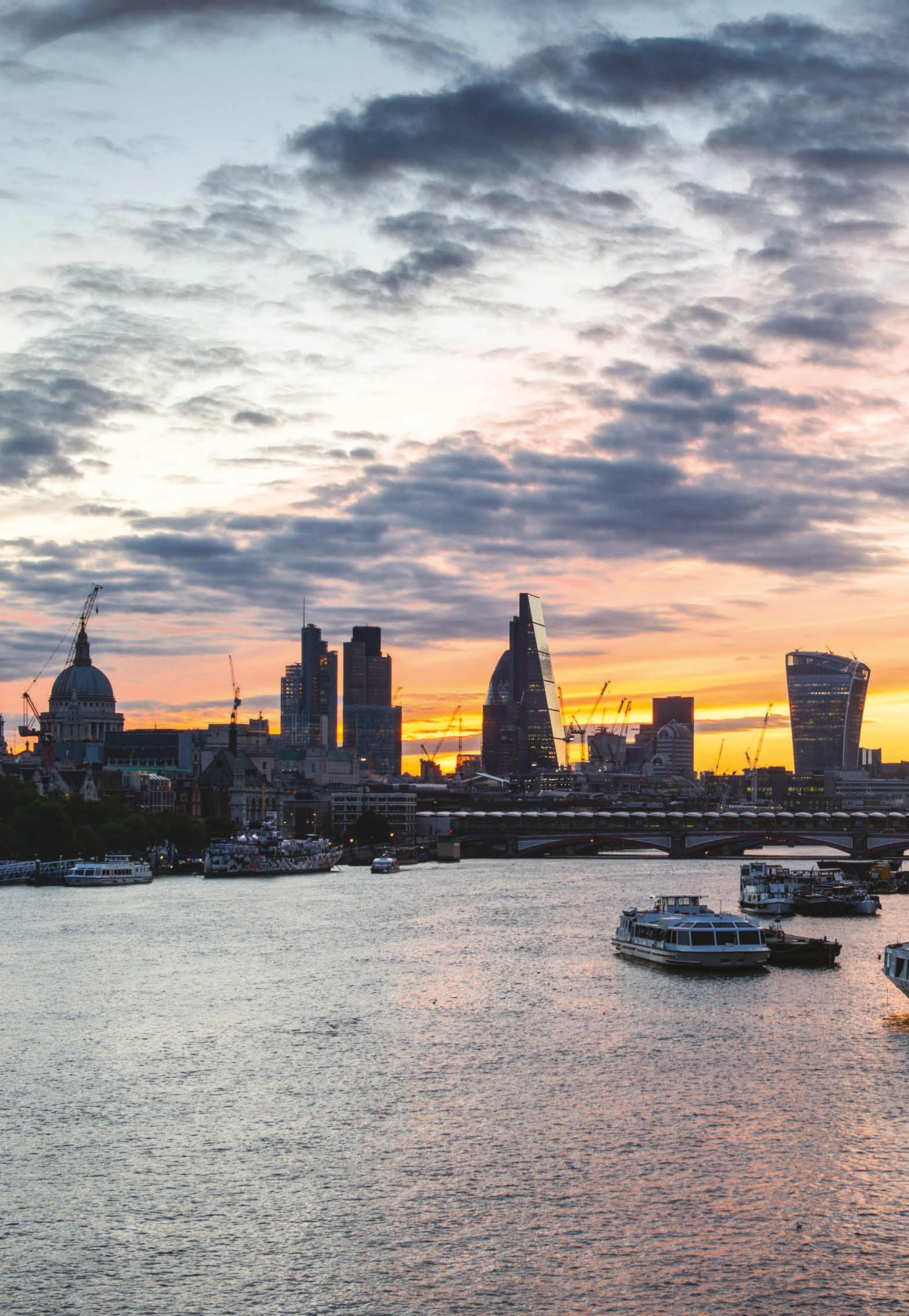
Legal Readiness for Climate Finance:

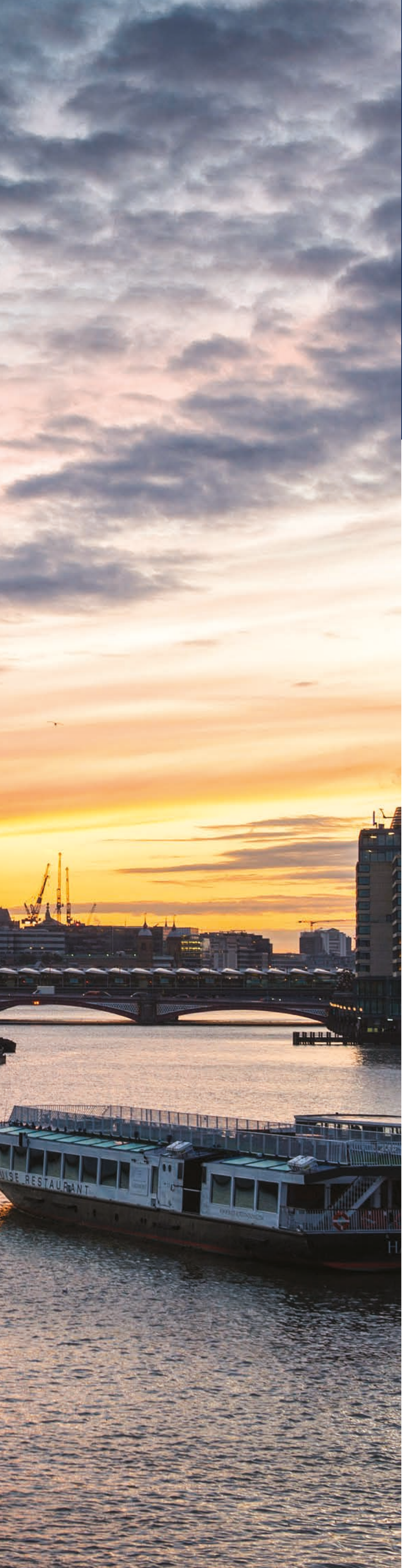
Private Sector Opportunities

Report and Findings of Roundtable held at King's College London, 25 January 2019

UN environment

United Nations Environment Programme





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1 Introduction

1.1 The legal challenge

Addressing climate change will require increased flows of private capital and more effective leveraging of public capital globally. The reason is simple: making the transition to a low-carbon and climate-resilient global economy will take vast sums of money that far exceed current government bursaries. As such, conceptions of 'climate finance' and 'sustainable finance' must now include private capital.

Efforts by the private sector will help countries to meet their obligations under the Paris Agreement; and capital-allocation decisions by the market will facilitate the transition (or not) to a low-carbon economy. Those efforts and decisions are shaped by law and regulation as well as policy. Having 'legal readiness' for climate finance can encourage investor confidence.

Specifically, legal readiness for climate finance includes:

- Laws and regulation that "can enable access to climate finance and investments and realise NDC [Nationally Determined Contribution] targets" and "that have been carefully considered and enacted based on comprehensive assessment, analysis and consultations" (Morita and Pak 2018: 11); and
- Building legal and institutional capacity through knowledge-sharing and technical expertise.

Legal readiness is relevant for all countries; yet it is especially pressing for developing countries. This is because it encourages not only increased flows of climate finance, but also transparency, clarity, and accountability of multi-stakeholders by providing the architecture for regulating behaviours and activities. Importantly, legal and regulatory frameworks can both 'call in' external (multilateral) climate-related funding and also 'put out' endogenous (in-country) investment opportunities (Bowman 2018a). So an important corollary of building legal readiness and capacity for climate finance is that it strengthens country ownership in financial processes for more sustainable outcomes.

This area is extremely new and key questions are just emerging. How can law-makers, regulators, and practitioners work together to support the implementation of the Sustainable Development Goals (SDGs) and the Paris Agreement? What is – and should be – the role of law and regulation for a truly systemic transformation by enabling finance at scale, encouraging project pipeline, and ensuring corollary benefits of enhancing economic and social development in a sustainable way?

This level and type of change presents a new challenge for many law-makers and regulators around the world. It also presents risks and opportunities for the private sector. Learning from the experiences of early-movers can help other countries to initiate legal and regulatory reforms to build critical mass for a global transformation.

Roundtable delegates

1.2 The roundtable: purpose and design

This report summarises the agenda and findings of the *Legal Readiness for Climate Finance: Private Sector Opportunities* roundtable co-convened by King's College London, UN Environment, and Legal Response International. It is part of an ongoing King's College London/UN Environment partnership to stimulate collaborations and mutual learning between public and private stakeholders in developing and developed countries for transformational change.

This roundtable is a sister event to *Climate Finance Law: Legal Readiness for Climate Finance* which was co-convened in March 2018 by King's College London and UN Environment (see Bowman and Steenmans 2018). It was aimed at the public sector and focused on experiences of Kenya and Mexico as case-studies. Delegates at that workshop subsequently indicated a strong desire to engage with the private sector, especially lawyers, financiers, and investors.

Thus, this 2019 roundtable embodies the next step in providing a forum in which public sector actors and private practitioners can learn from each other to increase collaboration and to strengthen national law and regulation to enable financial opportunities at scale.

The roundtable was held on 25 January 2019 at King's College London. It comprised 26 invited experts from the UK, Europe, and Kenya who are situated in the private sector (legal, financial, consulting), the public sector (central banks, financial regulators, multilateral financial institutions), specialist non-government organisations (legal and financial); and academia. Participating organisations are listed in Appendix A.

Roundtable delegates shared knowledge and experiences with the aims of:

- Identifying business opportunities alongside risks for practitioners in this space;
- Identifying concrete actions to improve the legal and regulatory enabling environment for private sector investment and implementation of NDC, Paris, and SDG objectives;
- Identifying emerging criteria that help central banks and other regulators engage the finance sector in their own jurisdictions;
- Institutional learning between participants from different sectors and countries; and
- Creating and shaping a new global community of decision-makers in Climate Finance Law.

In order to tease out and share learnings about the legal and regulatory dimensions of climate finance, the event was designed as follows:

It was structured around three main themes:

1. The regulators' role in sustainable finance leadership;
2. Designing a toolkit for law-makers and regulators; and
3. Opportunities for mainstreaming climate finance, especially in developing countries.

And it comprised two components:

A Full-day private roundtable as a forum for dynamic discussion under the Chatham House Rule of non-attribution. Lead speakers gave short presentations to kick off full group discussion and debate.

B Evening public event designed to bring awareness of key issues to a non-specialist public audience. A panel of roundtable delegates presented on the regulators' role, designing a legal and regulatory toolkit, and mainstreaming green finance, which was followed by audience Q&A.

Appendix B sets out a detailed agenda.

2 Framing: core themes

2.1 Session 1

In 2015 Mark Carney, the Governor of the Bank of England, was the first financial regulator to publicly herald that climate change presents systemic financial risks with potential to destabilise markets and induce a new global financial crisis. Since then central banks around the world have started paying attention to climate risk, with early-movers including France, China, and the Netherlands. Most recently, the Bank of England's Prudential Regulation Authority (PRA) released a Supervisory Statement for consultation in October 2018 setting out high-level (non-prescriptive) expectations for banks and insurers.

Climate change poses financial risks. Regulators are now starting to develop methodologies, analytical tools, and approaches to better equip the financial system to respond to it.

Moreover, the Banque de France has initiated the Central Banks and Supervisors Network for Greening the Financial System (NGFS) which is a voluntary network commenced with 8 founding institutions in December 2017. In a very short time it has expanded to more than 30 members and observers globally (Banque de France 2019). NGFS objectives include contributing to the development of climate risk management in the finance sector, mainstreaming finance to support the low-carbon transition, and defining and promoting best practices for in-country implementation by member banks. It also serves as an educational community whereby member banks can disseminate best practices and learnings with each other. It has three workstreams, each of which is chaired by a member institution. The workstreams are as follows:

1. *Supervision* (chaired by Bank of China): mapping regulatory and supervisory practices including disclosure by financial institutions;
2. *Macro-financial* (chaired by Bank of England): connecting climate change and financial stability; and
3. *Mainstreaming green finance* (Chaired by Deutsche Bundesbank, Germany): central banks/supervisors as catalysts for greening the financial system.

The NGFS published its first progress report in October 2018 which concluded that climate change poses financial risks; and that regulators have been lagging but are now starting to develop methodologies, analytical tools, and approaches to better equip the financial system to respond (NGFS 2018). In April 2019 the NGFS will provide its first comprehensive report on why climate change falls within the responsibility of central banks and supervisors, and their role in this regard. Other examples of international collaboration include the G20 Sustainable Finance Study Group; and initiatives for

capacity building in emerging markets such as the IFC-convened Sustainable Banking Network (SBN) and Global Green Finance Leadership Program.

Activity from regulators is a positive trend. Their leadership has potential to catalyse more ambitious and faster action.

Similarly, securities and financial markets' regulators around the world are beginning to step up focus on climate risk disclosure and to increasingly engage with firms. Early-movers include the French Financial Market Authority (AMF), the Dutch Authority for Financial Markets, the UK Financial Conduct Authority, and Japan's Financial Services Agency. The French AMF is an excellent example of regulatory innovation in this space. It is one of the first financial market authorities to publish a vision and roadmap for investor protection, information disclosure and transparency, and efficient and fair functioning of the market in the context of climate risk and opportunities (AMF 2018). This has included the creation of a new Strategy and Sustainable Finance Unit, which has been tasked with implementing the roadmap in the context of further legislative changes introduced by the new *French Action Plan for Business Growth and Transformation* (PACTE) corporate law reform. Moreover, the California Department of Insurance, the European Insurance and Occupational Pensions Authority, and also the UK Department for Work and Pensions have made clear that climate change is not a peripheral ethical issue but a strategic and financial risk issue. Many of these regulators are pushing for stress tests and scenario analyses for banks, insurers, and financial service providers, and even divestment of fossil fuel assets by regulated firms in the case of the Californian Insurance Commissioner.

Moreover, akin to the NGFS and given the growing momentum in this new area, a number of securities market regulators are starting to share knowledge about supervisory practices and market behaviours through international networks such as the International Organisation of Securities Commissions (IOSCO) and the European Securities and Markets Authority (ESMA).

These initiatives by financial regulators are relatively recent and highly innovative. Supporters view this "flurry of activity" from regulators as a positive trend given that their leadership has potential to catalyse more ambitious and faster action from the financial sector (Cripps 2018). Yet critics have warned against a perceived over-reach of regulatory mandate (Crow and Binham 2018).

To enable climate finance, there is an important role for regulatory leadership to facilitate not only external collaboration between public and private sectors but also internal collaborations between law-makers, policymakers, Treasury, and other Ministries with portfolios such as environment, transport, agriculture, and energy. Some developing countries are making this a priority. For example, Kenya exemplifies why both approaches are important. Due to the serious consequences of climate change it implemented recent national measures with a particular focus on climate finance, such as the *National Climate Change Action Plan 2013-2017*, the *Climate Change Act 2016*, and a *National Policy on Climate Finance 2018*. Yet despite this regulatory activity, the Kenyan Treasury has identified a need for more effective engagement with the private sector to locate climate-relevant targets/projects and apply for green funding from the finance sector as well as providing finance directly to fill public funding gaps. So the Kenyan Treasury is now focusing on how best to incentivise private investment, including structures to support public-private partnerships and tax incentives to encourage the entry of private investors. These changes will necessarily include strengthening the legal environment to improve investor confidence and attract private climate finance from developed countries. Accordingly, the Kenyan Treasury has highlighted a need for technical assistance and capacity building to help map and strengthen legal architecture.

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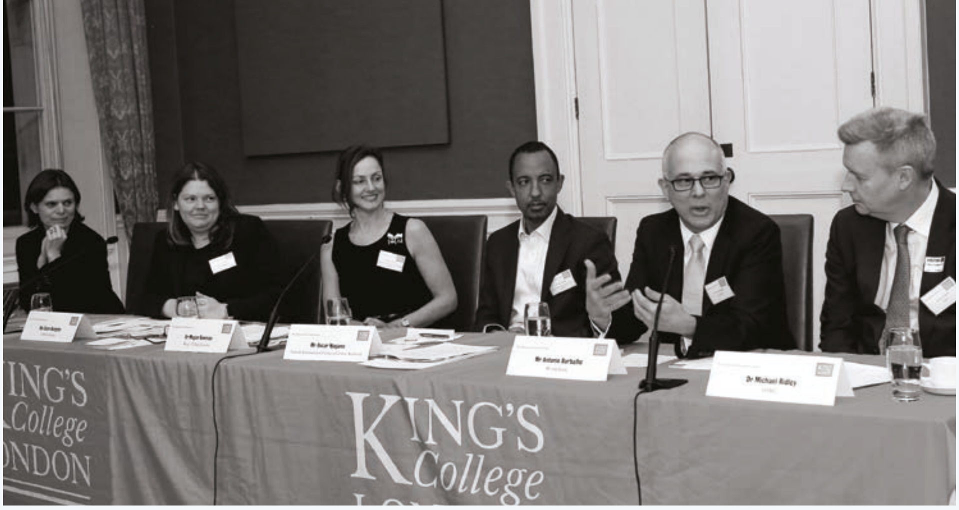

2.2 Session 2

It is important to consider legal and regulatory tools that can be utilised to enable climate finance at scale. Broadly, law and regulation can mandate or steer climate finance flows using a hard approach that mandates behaviour ('command and control' regulation) or through softer ways such as financial incentives/disincentives and disclosure. An important ingredient is establishing a common language or aim (e.g. through a taxonomy); and to be 'predictively flexible' in climate legislation.

More specifically, law-makers can utilise a two-fold typology of regulatory options and legal forms to mobilise climate finance through 'financial mechanisms' and 'facilitative modalities'.

(Bowman 2018a, 2018b).

Financial mechanisms directly mobilise or leverage private finance through, for example blended finance (grants, loans, guarantees, insurance), green investment banks, climate trust funds, carbon pricing, tax incentives, green bonds, feed-in tariffs, and subsidies. In contrast, facilitative modalities are non-financial initiatives that help indirectly mobilise private finance by improving knowledge transfer, project pipeline, and capacity building. This includes enhancing governance structures, prudential regulation, corporate reporting, matchmaking and training schemes, renewable energy targets, and taxonomies for defining 'green' investments. Both types of option are essential and complementary for creating an enabling regulatory environment. In particular the 'facilitative' category is rarely acknowledged as a component of climate finance, yet it is crucial for its success (Bowman and Steenmans 2018).