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ECO:FACT QUARTERLY

The briefing for E&S risk experts

The ECOFACT Quarterly is a briefing on environmental and social risks relevant for the financial sector. This sample report includes the editorial, excerpts from three tables, and a limited selection of 9 news items from the 41 items featured in the full report. For information on subscribing to the ECOFACT Quarterly, go to the **last page.**

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Editorial

It's All Change in 2020

One thing is certain: **2020 is going to see tremendous change in sustainable finance.** This will apply first and foremost to any financial institution with business ties to the European Union (EU). You'll also be surprised at **how little people in compliance, product development, and even investment departments know about the imminent changes** – unless they have a very strong ESG team. And even if they are up to date, it's unlikely that they will have the necessary technical expertise and data. This is a **huge opportunity for ESR/sustainability/ESG teams.**

The two key drivers of change:

- On December 9, 2019, the EU published the new Regulation on Sustainability-Related Disclosures in the Financial Services Sector.[1] **Our recent legal analysis** of the package resulting from the EU action plan for sustainable finance **shows that, depending on type, financial institutions are facing up to 300 action items.**[2] These apply to any financial institution that has a branch or subsidiary in the EU, manages an EU-based product, is seeking to acquire clients in the EU, or is selling products to them.

  By June 30, 2021, for example, financial market participants will have to publish information about **how they integrate sustainability risks** into their investment decision-making processes and investment or insurance advice. They will also have to publish statements on **how they take into account the principal adverse impacts**[3] on the environment and society resulting from their investment decisions – or explain why they do not.

- Equally importantly, **the European Green Deal[4]** announced on December 11, 2019 **finally provided us with an initial regulatory roadmap[5] for the real economy in Europe.** Late last year,[6] we explained why it was difficult for the financial sector to act on climate risk as long as such roadmaps were not available: it makes it practically impossible to predict transition risk and assess new market opportunities available to clients or investee companies. Now it will be easier.

If you have the opportunity, support the investment arm of your institution in developing policies, due diligence and assessment processes, as well as reporting and disclosure frameworks. It will be a game changer and provide the basis for work that will affect other products and services in a second phase.

'Happy New Year' from the ECOFACT team and all the best for an exciting and busy 2020!

Olivier Jaeggi, Gabriel Webber Ziero

1. Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (27 November 2019). On the same day, the EU also published Regulation (EU) 2019/2089 amending Regulation (EU) 2016/1011 as regards EU climate transition benchmarks, EU Paris-aligned benchmarks and sustainability-related disclosures for benchmarks (27 November 2019).
2. For further information, please contact one of our legal analysts at policy@ecofact.com
3. Please note that the concept of adverse impacts is closely aligned with how risk is used in the OECD Due Diligence Guidance for Responsible Business Conduct. In the words of the OECD, assessing "adverse impacts […] is an outward-facing approach to risk," focusing on assessing the likelihood of adverse impacts on people, the environment and society that an enterprise may cause – and not about risk for the investor or the financial institution itself. The Regulation (EU) 2019/2088 explicitly states that "financial market participants and financial advisers should consider the due diligence guidance for responsible business conduct" developed by the OECD.
4. The European Green Deal: https://ec.europa.eu/info/sites/info/files/european-green-deal-communication_en.pdf
5. As part of the New Green Deal, the EU has announced that it will review all regulations in order to align them with its climate goals; it will also propose the first European climate law and launch a new circular economy action plan by March 2020.
6. https://www.ecofact.com/downloads/ECOFACT%20Quarterly%20Issue%2027.pdf

Editorial
International standards
High-risk sectors
Emerging risks
Business case
Peer approach
New tools & databases
About
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*We will dedicate up to 10 hours to the assessment. There may be a waiting list.

"Useful and much-appreciated report among Swiss Re's ESG experts."
Swiss Re

"Well-prepared, practical information that meets our needs in addressing environmental and social risks."
UniCredit Group

"Very well done, and extremely useful for our daily work."
Commerzbank

International standards

Updates on cross-sector environmental and social standards which might be relevant as a benchmark for risk assessments.
Scope: key developments related to the most important international environmental and social standards.

→ New OECD Guidance for Banks on Due Diligence for Responsible Corporate Lending and Securities Underwriting

The OECD's new guidelines were developed together with a multi-stakeholder advisory group of more than 50 organizations and endorsed by 48 countries. The document defines expectations regarding due diligence for the business at the heart of the banking industry. It is the first document to broadly recognize environmental and social standards for corporate lending and underwriting transactions, although these transactions represent the vast majority of banking finance activities. The paper goes beyond the climate discussion, addressing the entire spectrum of the Sustainable Development Goals (SDGs). October 29, 2019.

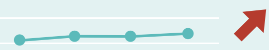
ECOFACT is proud to have contributed to these important guidelines. If you want to know more, please to not hesitate to contact us as at **info@ecofact.com** or **+41 44 350 60 60**.

Read more (1) → Read more (2) → Read more (3) → The report →

Coming soon:	Expected by:
ISO/WD 32210 Framework for sustainable finance: Principles and guidance	Under development. No time plan publicly available.

High-risk sectors

Developments relevant to six specific high-risk sectors, such as news on risk factors and trends, the relevant regulations, and best practices. The table below contains an update on controversies, and comments on the corresponding reputational risk for financial institutions.

		Information based on RepRisk data		Analysis based on RepRisk data, combined with insights gained in ECOFACT's consulting practice	
		RepRisk runs the most comprehensive database on environmental, social and governance (ESG) risk. RepRisk systematically collects and analyzes negative incidents, criticism, and controversies about companies and projects worldwide, and offers information on activities related to human rights violations, breaches of labor standards, corruption, environmental damage, and violations of international standards. www.reprisk.com		The grades take into consideration the degree of reputational risk to financial institutions that is associated with investments in the subsectors mentioned. **An "A" indicates that transactions related to this topic present comparably low reputational risk, while an "E" indicates high reputational risks.**	
		Level of controversies # of RepRisk risk incidents per quarter and trend of the last three months† DJF MAM JJA SON	**FI exposure** Share of news criticizing banks and / or insurers	**ECOFACT summary**	**ECOFACT risk rating**
Agriculture	Palm oil	 42%	10%	The palm oil sector is associated with issues such as deforestation, threats to endangered species, and poor working conditions. While, "No Deforestation, Peat, Exploitation" (NDPE) commitments by RSPO members have been criticized for a lack of on-the-ground verification, FIs are urged to request NDPE commitments from their clients and to monitor compliance. FIs lacking stringent palm oil policies or involved with companies that do not adhere to best practices face considerable reputational risks.	D
Utilities	Coal-fired power	 8%	7%	Coal-fired power remains highly controversial due to its impact on human health and the environment, and particularly to its contribution to climate change. FIs involved in financing coal-fired power plants or with clients associated with the coal industry are frequently targeted by NGOs. Increasing numbers of FIs are distancing themselves from coal-fired power projects and companies.	E

†The green / red arrows mean that the number of RepRisk risk incidents has fallen or risen by more than three risk incidents in the last three months, whereas the orange arrow means that the change in the number of RepRisk risk incidents in the last three months has been smaller than three. *Indicates a change in the ECOFACT risk rating compared to the previous quarter.

High-risk sectors

Oil & Gas | Mining | Forestry | Agriculture | Utilities | Chemicals | Other

Risk factor

Nickle mining for electric vehicle batteries causing environmental destruction in Indonesia

With the popularity of electric vehicles driving demand for batteries to power them, millions of tons of nickel and its derivatives will be required over the coming decades. Indonesia is particularly rich in nickel deposits, which are close to the surface and concentrated at twice the levels found in other countries such as Australia. Environmental advocates are warning that nickel mining in Indonesia is already negatively affecting livelihoods and ocean ecosystems, and is resulting in massive toxic slag piles. Continued development of the industry could entail irreparable damage to the environment and further degradation of residents' quality of life and health. There are currently 11 nickel smelters around the country, 25 mine-smelter combinations slated to open by 2022, and thousands of nickel mines. The actual number is unknown, as many are illegal. The country is notorious for its corruption, and human rights campaigners are concerned that "police, army and government will continue to collaborate to evict residents" if their villages are on top of mineral deposits. November 20, 2019.

Read more →

Risk factor

Brazilian government seeks to allow mines on indigenous reserves

The Brazilian government has presented a bill that will open the door to more mining operations countrywide, including on indigenous lands. The Mines and Energy ministry announced in July that it was forming a working group charged with simplifying Brazil's mineral prospecting process. Reflecting those efforts, this latest bill will legalize many of the small-scale, independent wildcat mines that are currently operating illegally. Brazil's Bolsonaro-led government has also sought to open indigenous reserves to mining, logging, and farming interests, a move that observers say helped to feed the fires that swept through the Amazon rainforest earlier this year. October 3, 2019.

Read more →

Risk factor

RSPO forces consumer giants to adopt green alternatives

The Roundtable on Sustainable Palm Oil (RSPO) is set to penalize consumer goods makers who fail to transition to green palm oil. Palm oil production is devastating Southeast Asian forests, largely due to the slash-and-burn deforestation techniques that continue to cloak Singapore, Malaysia, and Indonesia in smog. Green growers say that their cleaner, but more expensive crop has failed to sell, so RSPO has opted to force consumer goods makers like Unilever and Nestle to buy larger quantities of green palm oil. RSPO members such as consumer companies, retailers, traders, and palm growers must now increase their sustainable purchases by 15 percent annually or face fines and possible suspension. Large consumer firms have pledged to use green palm oil in their products, but warn that there are also sustainable supply reliability and transportation issues to overcome. October 16, 2019.

Read more →

Emerging risks

Risks that may become material in the near future or are relevant when looking into a company's business model, but are not yet considered as highly significant risks from a financial institution's reputational risk perspective, or are not related to a high-risk sector.

Air pollution

→ **Research links air pollution to aggressive behavior and violent crime**

Analysis of three 2006–2013 US government data sets by American researchers revealed a same-day link between a rise in fine-particulate air pollution and violent crimes, the vast majority of which were assaults. If fine particulate matter levels (PM2.5) increased by 10 micrograms per cubic meter in a single day, violent crimes increased by 1.4 percent. If ozone exposure increased by 0.01 parts per million in one day, an increase of 0.97 percent in violent crime or a 1.15 percent increase in assault resulted. Further calculations determined that if daily PM2.5 levels could be reduced by 10 percent, more than USD 1.1 million in crime costs could be saved each year. Researchers checked for other possible explanations for this finding, such as weather, heat waves, precipitation, and other general factors at county level. Air pollution levels have also been linked to increased levels of the stress hormone cortisol in the human brain. October 9, 2019.

Read more (1) → Read more (2) → Read more (3) →

Business case

Information that underlines the business case for environmental and social risk management in financial institutions.

➔ New Jersey tackles gun control in a unique way – leveraging relationships with banks and gun retailers

Faced with federal inaction to address gun control in the US, as well as mass shootings and gun violence, the State of New Jersey has expanded (via executive order) its already rigorous firearms purchase background checks, placed restrictions on retailers selling to the state's law enforcement agencies, and will require vendors and financial institutions to adopt its policies to maintain eligibility for state contracts. The governor's announced plan was short on details but expected to include suggestions from gun control groups, including enhanced training for retail workers, electronic record-keeping requirements, and background check services for private gun sellers. The state claims that it pays USD 1 billion in bank fees annually and spent USD 70 million on firearms and supplies for law enforcement in the space of a few years, suggesting that it has significant clout to alter practices on a wider scale. The state is encouraging others to pursue similar tactics in other jurisdictions. September 10, 2019.

Read more ➔

➔ EU Taxonomy to bring regulation to the unregulated world of green finance

Currently under development by EU officials, a taxonomy to define standards for green investments and to prevent "greenwashing" could become a benchmark for green finance that extends outside the EU. Green finance, which is currently estimated to be worth USD 30 trillion, is largely unregulated around the world. The expert group creating the taxonomy has so far set criteria consistent with the Paris Climate Agreement requirements for almost 70 economic activities. The anticipated requirements of the imminent regulations could have a "massive" impact globally, and some investors are already using the draft criteria to evaluate their portfolios. Hoping to channel more funds into green finance to advance climate mitigation, the taxonomy will also inform the EU green bond standard and other product labels. A draft text of the EU Sustainability Taxonomy Regulation that incorporated compromises for all branches of the government was finalized in December 2019. It is understood that the EU Council and the EU Parliament have agreed that the EU Sustainability Taxonomy Regulation's requirements would apply starting in December 2021. November 27, 2019.

Read more ➔ Proposal ➔

ECOFACT Policy Outlook users can find additional information on the EU sustainability taxonomy **here**. Policy Outlook, a monitoring and implementation package, covers regulatory change pertaining to ESG and corporate responsibility issues. Click **here** for further information.

Peer approach

New sector and issue policies that financial institutions have recently adopted. The table below gives an overview of the number of sector and issue policies produced by financial institutions.

Banks

➔ BNP Paribas publishes timeframe for coal exit

BNP Paribas has confirmed that it will continue to fund world coal until 2040 and the thermal coal sector in the European Union until 2030. It also aims to strengthen support for renewable energies, with a target of EUR 18 billion by 2021. In 2015, BNP Paribas committed itself to matching its investment activities with the Paris Agreement. In 2017, it ceased backing new coal-fired power plant projects and those companies whose chief income derives from non-conventional hydrocarbons. In line with the Sustainable Development Scenario (SDS) of the International Energy Agency (IEA), BNP Paribas aims to cut the CO_2 intensity of its worldwide electricity mix by 85 percent by 2040. The Group will continue to publish target results annually. November 22, 2019.

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Editorial
International standards
High-risk sectors
Emerging risks
Business case
Peer approach
New tools & databases
About
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Sector and issue policies adopted by insurers

(A) indicates the number of insurers among the 9 Systematically Important Insurers which have adopted a policy, guideline, or commitment addressing the corresponding sector or issue for their investments. (B) indicates the number of insurers which have adopted a policy, guideline, or commitment addressing the corresponding sector or issue in underwriting. Only the sectors or issues covered by policies are included in the table.

Sector policies	A	B
Agriculture	2	1
Palm oil	2	1
Tobacco	3	2

Issue policies	A	B
Climate change	6	4
Agricultural commodities	2	1

This table includes the 9 global systemically important insurers (G-SIIs) according to the Financial Stability Board: Aegon N.V., Allianz SE, American International Group, Inc., Aviva plc, Axa S.A., MetLife, Inc., Ping An Insurance (Group) Company of China, Ltd., Prudential Financial, Inc., Prudential plc. Source: **fsb.org**

Sector and issue policies adopted by banks

(C) indicates the number of banks among the 30 Systematically Important Financial Institutions which have adopted a policy, guideline, or commitment addressing the corresponding sector or issue and disclose its content. (D) indicates the number of banks which disclose that they have adopted a policy, guideline, or commitment, but do not disclose the corresponding content.

Sector policies	C	D
Agriculture (general)	8	5
Biofuels	3	2

Issue policies	C	D
Biodiversity	1	3
UNESCO World Heritage Sites	18	1

This table includes the 30 Systematically Important Financial Institutions (SIFIs) according to the Financial Stability Board: Agricultural Bank of China, Bank of America, Bank of China, Bank of New York Mellon, Barclays, BNP Paribas, China Construction Bank, Citigroup, Credit Suisse, Deutsche Bank, Goldman Sachs, Groupe Crédit Agricole, HSBC, Industrial and Commercial Bank of China Limited, ING Bank, JP Morgan Chase, Mitsubishi UFJ FG, Mizuho FG, Morgan Stanley, Nordea, Royal Bank of Canada, Royal Bank of Scotland, Santander, Société Générale, Standard Chartered, State Street, Sumitomo Mitsui FG, UBS, Unicredit Group, Wells Fargo. Source: **fsb.org**

New tools and databases

This section presents new tools and databases that can help to identify or manage environmental and social risks.

PRI tool forecasts “forcible, abrupt” policy response to climate change, highlighting investor risk exposure

The Inevitable Policy Response (IPR) tool is headed by the Principles for Responsible Investment (PRI) in partnership with Vivid Economics and Energy Transition Advisors. It predicts a global “torrent” of “forceful, abrupt, and disorderly” policy change as early as the mid-2020s, as governments attempt to respond to increasing impacts of climate change. Investors are warned against complacency and encouraged to act now to determine risks to their portfolios as “[t]he greater the delay in responding, the greater the potential cost.” The IPR forecasting tool is promoted as a business planning case replacement for the International Energy Agency’s (IEA) New Policy Scenario (NPS) to be used by investors, corporates, and regulators. It will be continually updated to reflect developments, but the tool’s early predictions include peak coal around 2022, oil in 2028, and natural gas near 2040, and almost all the world’s electricity will be produced by renewables by 2050. September 24, 2019.

Read more (1) → **Read more (2)** → **Read more (3)** → **IPR briefing** →

About this report

This briefing is tailored to the needs of individuals and teams in charge of assessing and controlling environmental and social risks in corporate banking, investment banking, and commercial insurance. It aims to provide an update on risks, standards, tools, and best practices that are relevant primarily from a reputational risk perspective.

The content is organized into four levels: each item of information is headed by a title which allows the reader to digest the report in less than five minutes. Subsequently, a brief abstract summarizes the key facts. Additionally, if appropriate, a short comment illustrates why this information might matter and, finally, a link to the original source allows the reader to drill down further into the subject.

Our research process consists of four steps: firstly, ECOFACT collects information from international newspapers and specialized periodicals. Secondly, the websites of the most relevant NGOs, international organizations, private and academic research centers, environmental and sustainability think-tanks, and government agencies are visited regularly. Thirdly, specialized newsletters to which we subscribe are screened, and finally, organizations in charge of international environmental and social standards are contacted.

Selection criteria for the content of the briefing: a) information on environmental and social risks that b) was published (in most cases) over the past quarter, and c) is relevant from the reputational risk perspective of a financial institution. The scope covers the ten principles of the UN Global Compact.

About ECOFACT

ECOFACT has addressed the risks and opportunities that environmental, social and governance issues present to the financial sector since 1998. We work primarily for banks, insurers, institutional investors, and international standard-setters.

We help our clients to improve their understanding of credit, reputational, compliance and liability risks in the context of sustainability, ESG and responsible business conduct.

Due Diligence

We assist our clients in designing processes and conducting due diligence:

We provide solutions for issue monitoring, policy development, portfolio screening, individual risk assessment, and engagement services.

Research Products

In addition to the *ECOFACT Quarterly,* ECOFACT also produces the *Policy Outlook.* The *Policy Outlook* covers regulatory change pertaining to ESG and corporate responsibility issues. It a monitoring and implementation package that consists of an online tool and provides access to a network of peers.

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Knowledge Sharing

ECOFACT hosts three events that facilitate knowledge sharing among peers and experts:

- The *Policy Outlook Conference* gives you the chance to join peers and experts from the fields of public policy, legal & compliance, corporate responsibility and sustainability in exploring how financial firms are addressing corporate responsibility regulations.
- The *Environmental and Social Risk (ESR) Roundtable* provides an opportunity for peers to discuss the challenges that arise as environmental and social issues are further integrated into financial institutions' business with corporate clients.
- The *Reputational Risk Management (RRM) Roundtable* is a platform for dialog and knowledge sharing on common and best practices in reputational risk management in the financial sector.

ECOFACT is a signatory to the *United Nations Global Compact* and the *Principles for Responsible Investment,* and a member of *Swiss Sustainable Finance.*

Swiss Sustainable Finance | The Global Compact – We Support | PRI Principles for Responsible Investment

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