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Yann Pouëzat

Director for Corporate Financing and Financial Markets, French Treasury, Ministry of Economy and Finance, France

Policies challenges for addressing standardized ESG adoption

Since the Paris Agreement in 2015, various institutional and normative initiatives have emerged to foster more transparency and long-termism in the economy. The fight against climate change requires to involve the financial system into the path of energy transition.

The ambition to redirect financial flows towards a more sustainable economy has been partly made more tangible. However, the absence of convergence around a common definition of 'sustainability' prevents companies from appropriately disclosing the degree of environmental sustainability of their economic activities. In this regard, the future adoption of the European Taxonomy in 2020 - classifying the economic activities regarding their sustainable impact - has a strategic role to play in helping investors define their investment policies accordingly. Thus, this common language and the associated regulatory efforts are essential to tackle the existing challenges regarding the corporate issuer's disclosure of environmental, social and governance (ESG) information and consequently sustainable investing.

The European Union, through its Action Plan for sustainable finance has incorporated some new reporting requirements on the sustainable impact of investments in the existing regulations applying to financial markets. However, the multiplicity of non-comparable ESG information reflects the different approaches to corporate issuer disclosure and scoring system frameworks. European public policy initiatives shall help to streamline the number of different corporate disclosure frameworks which – as strong as they may appear – blur the readability of the ESG information among different corporate issuers and incur significant costs. By delivering some proportionate policy measures to corporate issuers, the EU shall focus, as first step, on promoting a better global alignment of the different ESG indicators. Nonetheless, the normative character of the EU future policies will have to avoid the risk of excessive granularity and the restriction over investors or rating agencies' innovation upon indicator measurements.

This common sustainable reporting framework makes it necessary to adapt this requirement to the capacity of each corporate issuer. As clear disclosure from small and mid-caps becomes scarce, the reliance by investors or insurers on every kind of data can give rise to a somewhat misleading image of smaller companies' ESG criteria adoption. The establishment of a pragmatic common reporting framework consistent with corporate issuers' resources is a key success factor for the development of sustainable investment.

The common objective to achieve a higher quality and comparable ESG data cannot be disconnected from the ambition to adjust our real economy. Europe must be able to respond to the concrete expectations of its citizens with regard to the energy transition. To this end, the social dimension, as one of the pillar of the ESG criterias, should be acknowledged through the simplicity of the ambitious framework required. This makes it necessary to take into account operational complexities for the incorporation of ESG information in order to consider the sustainability impact as a key element of the corporate strategy. ●