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WBA Releases First Financial System Benchmark

June 13, 2023

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In May 2023, the World Benchmarking Alliance (WBA) **released a report** on the first edition of its **Financial System Benchmark**, which assesses financial institutions' progress toward climate change goals. The WBA is a non-profit organization which aims to develop a variety of benchmarks to assess and rank "the world's most influential companies" on their contribution to meeting the United Nations' Sustainable Development Goals (SDGs). The benchmark, which WBA launched at COP27 in November 2022, assesses and ranks the 400 "most influential" or "keystone" financial institutions worldwide — those "with disproportionate influence on the structure and function of the systems within which they operate" — on their contribution to global sustainability transition goals, such as the SDGs and the Paris Agreement. The financial institutions assessed include banks, asset owners such as pension funds, development finance institutions (DFIs), sovereign wealth funds, asset managers, including alternative investor entities such as private equity, venture capital and hedge funds, and insurance companies.

The institutions were **assessed across three areas**:

1. Governance and strategy (40% of the total score), using five indicators: impact management and strategy, senior leadership accountability and remuneration, gender equality and diversity, engagement policy, and public policy engagement;
2. Respecting planetary boundaries (30% of the total score), using nine environment- and climate-related indicators, five on alignment with the Paris Agreement (financed emissions, financed emissions targets, engagement aligned with a 1.5° C trajectory, climate solutions and approach to fossil fuel sectors) and four on nature and biodiversity (nature and biodiversity-related impacts, protection and restoration of nature and

biodiversity through finance, protection and restoration of nature and biodiversity through engagement, and nature- and biodiversity-related solutions); and
3. Adhering to societal conventions (30% of the total score), using 18 indicators related to human rights.

The report highlighted seven key takeaways:

1. The entire financial system scores poorly on governance and climate. Although there are “no notable overall outliers,” some financial institutions have made progress in certain areas and can stand as examples for others.
2. The entire system is lagging on the approach to fossil fuels, a “contentious issue” that requires “stronger multi-stakeholder collaboration” and more transparency.
3. Financial institutions that have “gender-balanced boards” outperform those that do not across all climate-related indicators.
4. Financial institutions that tie executive compensation to sustainability also outperform across all climate indicators.
5. Stronger regulations result in greater transparency, which in turn leads to better performance across climate indicators.
6. Asset owners that are regarded as “important influencers” lack transparency and score poorly on climate-related indicators.
7. Despite often being at the forefront of financing climate solutions, private equity and venture capital are typically outside the scope of “mainstream regulations,” lack transparency and score poorly on climate indicators.

The WBA report offers specific recommendations for stakeholders, including regulators, standards organizations, activists and financial institutions themselves, as well as five overarching calls to action:

1. Board responsibility and top-down leadership for climate and sustainability actions are essential.
2. Gender-balanced boards and leadership go beyond equity considerations by positively impacting climate-related and sustainability decision-making.
3. Financial institutions must recognize their influence and commit to positively changing the financial system from within.
4. Wide-ranging transparency in climate disclosures is critical to financial system transformation, in particular around climate-change solutions.
5. Given WBA’s assessment that no institutions had “an adequate approach to phasing out all fossil fuels,” collaboration among all stakeholders is necessary to tackle this complex issue.

Taking the Temperature: The financial services industry remains at the center of numerous climate-related issues and challenges, including concerning emissions financing, financial system stability and regulatory capital requirements, as well as having to navigate “anti-ESG” forces in the U.S. While banks increasingly are voluntarily establishing emissions financing reduction targets and strategies, as are some insurers, at least some financial institutions have been subject to litigation and shareholder activity about their absolute climate commitments or the adequacy of plans to meet articulated targets.

Meanwhile, regulators remain concerned about whether financial institutions are adequately assessing and disclosing climate-related risk, and about overall financial system stability. Recent examples include studies on these issues conducted by the Bank of England and the European Central Bank; guidelines issued by Canada's Office of the Superintendent of Financial Institutions on climate risk management applicable to insurers and financial institutions; and guidance from the New York Department of Financial Services for New York domestic insurers on managing the financial risks from climate change.