REPORT

NEW CLIMATE INSTITUTE

FIXING THE BROKEN GOVERNANCE CHAIN

Aligning Private Finance with the Paris Agreement

AUGUST 2025

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Acknowledgements

This report is prepared by the ACHIEVE project, funded by the European Union's HORIZON EUROPE Research and Innovation Programme under grant agreement No. 101137625 to strengthen and scale high-integrity voluntary climate action for net-zero emissions by mid-century. We sincerely thank Takeshi Kuramochi, Silke Mooldijk, Derik Broekhoff, Natasha Chaudhary, and Lucie Pinson for their valuable insights.

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Citation

NewClimate Institute (2025). Fixing the Broken Governance Chain: Aligning Private Finance with the Paris Agreement. Available at: https://newclimate.org/resources/publications/fixing-the-broken-governance-chain-aligning-private-finance-with-the-paris

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EXECUTIVE SUMMARY

The climate governance chain in the financial sector is fundamentally broken. Despite growing awareness of climate risks and an increasing number of net-zero commitments, the sector remains structurally unfit to support a transition to a Paris-aligned economy. The key actors within the governance chain – comprising financial institutions (FIs), climate cooperative initiatives (CCIs) and regulators – have thus far failed to deliver the coordination, ambition and accountability needed. In its current form, the financial sector is unlikely to align with the Paris Agreement, let alone act as an enabler of the low-carbon transformation.

The symptoms of this breakdown are already visible. Financial institutions continue to channel capital into high-emissions sectors, with an estimated USD 3.7 trillion annually flowing into fossil fuels like oil, gas and coal (World Economic Forum, 2023). Climate cooperative initiatives (e.g. GFANZ) have largely failed to translate pledges into tangible decarbonisation outcomes in the real economy. Regulators and market environments, even in jurisdictions with greater attention to climate change, have not created the incentives and rules necessary to promote a shift to Paris-aligned finance. In some jurisdictions, climate alignment in the financial sector is even actively undermined.

Each actor in the governance chain bears responsibility for aligning financial strategies, portfolios and capital flows with the transition to a net-zero, climate-resilient economy. Structural barriers, such as the difficulty of pricing long-term climate risks and the challenges of coordinating collective action, can be addressed through complementary levers across the governance chain. Climate cooperative initiatives can mobilise and coordinate voluntary action, while regulators are positioned to correct market failures and establish effective incentives through targeted interventions.

To repair the broken climate governance chain, all actors must activate the levers within their discretion to overcome structural barriers, coordinate ambition and enforce accountability. To support that effort, this report examines the limitations of current climate governance in the financial sector and explores how financial institutions, climate cooperative initiatives and regulators can better align their actions with the goals of the Paris Agreement. It maps the key levers available to each actor, highlights where these remain underdeveloped, and provides a structured framework for action, ranging from minimum to high-ambition strategies, to guide more effective climate governance.

Based on our analysis, we propose the following recommendations for each actor in the financial sector (**see → Chp. 2** for the detailed analysis of levers for FIs, **see → Chp. 3** for CCIs and **see → Chp. 4** for regulators):

FOR FINANCIAL INSTITUTIONS

Minimum ambition level

- **Engage with escalation:** Establish clear, time-bound engagement strategies with escalation mechanisms for high-emitting clients and investees, focused on credible transition plans. Disclose engagement goals, progress, voting records and voting intentions on key climate resolutions.
- **Apply exclusion criteria:** Implement robust screening for sectors unlikely to transition and become Paris-aligned, such as coal, unconventional fossil fuels and deforestation-linked activities. Apply consistent standards across all material asset classes.
- **Ensure consistent and transparent reporting:** Report green and transition finance in line with established taxonomies to minimise risks of greenwashing and prevent mislabelling and opacity in finance disclosures. Condition transition finance on credible and verifiable transition plans.

Targeted ambition level

- **Channel capital to transition:** Scale positive ESG screening to actively channel capital towards green and transition finance. Deploy innovative finance tools such as blended finance to support impact-oriented strategies that go beyond traditional risk-return expectations.
- **Commit to advancing systemic change:** Publicly disengage from anti-climate lobbying efforts, limit participation in obstructive associations and actively support progressive climate policies.

FOR CLIMATE COOPERATIVE INITIATIVES

Minimum ambition level

- **Create action-based criteria:** Make membership criteria conditional on specific, verifiable actions (e.g. engagement and stewardship guidelines and targets, fossil fuel phase-out commitments, transition finance mobilisation thresholds), not just portfolio decarbonisation targets.
- **Enhance transparency and accountability:** Publish regular, independent assessments of members' progress and delist institutions that fail to comply.

Targeted ambition level

- **Strengthen governance:** Adopt hybrid governance structures involving public and civil society actors to shield climate cooperative initiatives from vested interests seeking to dilute ambition.
- **Bridge to regulation:** Actively promote the adoption of voluntary standards into mandatory regulatory frameworks through collaboration with policymakers.

FOR REGULATORS

Address gaps in Paris-Aligned regulation

- **Promote a rethink of fiduciary duty:** Expand definitions to explicitly include long-term climate risk and double materiality, providing legal clarity and protection for enabling climate-conscious investment decisions.
- **Integrate climate into prudential rules:** Revise prudential regulation to reflect climate risk through tools (e.g. capital requirements, sectoral exposure limits and mandatory stress tests).
- **Close the policy gap:** Align real-economy and financial regulations to ensure consistent signals that enable financial institutions to implement credible transition plans and align portfolios with climate goals.

Enable market-wide climate alignment

- **Scale de-risking tools:** Expand public instruments like blended finance and guarantees to lower the cost of climate-aligned investment, particularly in high-risk or emerging markets.
- **Deploy green monetary policy:** Move beyond 'market vneutral' approach by using instruments, such as climate-adjusted collateral frameworks and targeted asset purchase, to steer capital flows towards climate-aligned investments and reflect systemic climate risks.

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ABBREVIATIONS

ACHIEVE	Achieving High-Integrity Voluntary Climate Action
AM	Asset Management
AOA	Asset Owner Alliance
AUM	Assets Under Management
BoE	Bank of England
CA100+	Climate Action 100+
CCI	Climate Cooperative Initiative
CSDDD	Corporate Sustainability Due Diligence Directive
EC	European Commission
ECB	European Central Bank
EIB	European Investment Bank
ESG	Environmental, Social, and Governance
EU	European Union
EUR	Euro (currency)
FI	Financial Institution
FMLC	Financial Markets Law Committee
G20	Group of Twenty (international economic forum)
GBP	British Pounds (currency)
GDP	Gross Domestic Product
GFANZ	Glasgow Financial Alliance for Net-Zero
GIB	Green Investment Bank
IPCC	Intergovernmental Panel on Climate Change
MW	Megawatt
NDC	Nationally Determined Contribution
NGFS	Network for Greening the Financial System
NZAM	Net Zero Asset Managers initiative
NZAOA	Net-Zero Asset Owner Alliance
NZBA	Net-Zero Banking Alliance
NZIA	Net-Zero Insurance Alliance
OECD	Organisation for Economic Co-operation and Development
PRI	Principles for Responsible Investment
SFDR	Sustainable Finance Disclosure Regulation
SRI	Socially Responsible Investing
TCFD	Task Force on Climate-related Financial Disclosures
TNFD	Task Force on Nature-related Financial Disclosures
UK	United Kingdom
UKIB	UK Infrastructure Bank
UN	United Nations
US	United States
USD	United States Dollar (currency)

/∧ 01 INTRODUCTION

BACKGROUND

The global transition to a low-carbon economy by 2050 represents one of the most significant challenges of our time. Achieving net-zero CO_2 emissions by mid-century requires an estimated investment of USD 275 trillion, translating to around USD 9.2 trillion annually (McKinsey Global Institute, 2022). This represents on average 7.5% of global gross domestic product (GDP) over the next three decades. COP29's outcome positions the private sector as significant in closing this finance gap (WRI, 2024).

Despite this monumental need for green investments, private sector financing is still heavily skewed toward fossil fuels, with approximately USD 3.7 trillion annually flowing into GHG emission-intensive infrastructure, such as oil and gas extraction and coal production (World Economic Forum, 2023). This persistent investment in fossil fuels contrasts sharply with the urgent need to transition to low-carbon alternatives and highlights the financial sector's inaction to pivot decisively towards Paris-aligned finance.

Compounding this challenge, flagship initiatives designed to steer financial institutions toward climate action, including the Glasgow Financial Alliance for Net Zero (GFANZ) initiatives, have yielded to pressures from stakeholders with vested interests in preserving the status quo. Several major players that had previously made strong commitments have since withdrawn from the alliance (Phillips, 2023), while more ambitious members increasingly challenge the credibility of a coalition where members continue to finance fossil fuels (McNally, 2023).

Meanwhile, in the United States, the rise of the anti-environmental, social, and governance (ESG) movement reflects a growing scepticism about the financial sector's responsibility for the low carbon transition, exacerbating the global outflow of capital from ESG funds (Engler, 2024; Temple-West, Patrick; Schmitt, 2024). The Trump administration's economic strategy, characterised by deregulation, tax cuts, and backing for conventional industries, will likely further scrutinise the role of ESG in the US market (Boyapati, 2025).

Private financial institutions' (hereafter FIs) reluctance to stop fossil fuel finance and move capital to green and transitional activities seems paradoxical, as they intrinsically depend on long-term economic stability, which is increasingly threatened by climate change. While we observe some early promising practices of impactful climate action, we conclude that voluntary action alone is insufficient to drive systemic change in the financial sector. We argue that FIs should have a vested interest and a fiduciary responsibility to address the systemic risks linked to climate change with their financial management, but that it needs regulatory support to provide the guardrails and market incentives to align the financial sector with the Paris Agreement.

THE FINANCIAL SECTOR'S CLIMATE ACTION GOVERNANCE CHAIN

This report analyses the three main actor groups that form the governance chain determining the alignment of financial decision-making with the Paris Agreement: individual FIs, voluntary cooperative initiatives, and regulatory bodies. → **Fig. 1** illustrates this governance chain. At each of these three levels, we analyse barriers to impact and levers of impact, as well as promising practices that can contribute to reducing emissions in the real economy and advancing broader economic transformation. Where such levers and practices are not yet established, we underscore the need for the development of new approaches.

The effectiveness of the governance chain depends on the presence and interaction of all three interconnected levels. The first level **(see → Chp. 2)** is particularly critical, as it holds the main levers that private FIs (i.e. banks and asset managers) have to directly influence emissions in the real economy. FIs bear the responsibility for their facilitated and financed emissions and have the capacity to allocate capital and to exercise corporate stewardship over their investee companies. However, their ability to deliver meaningful climate action is often constrained by limited resources, restricted influence, information asymmetries, and profit-maximising mandates.

Non-state and state actor financial climate initiatives **(see → Chp. 3)**, which serve as collective organisations of financial actors united by a common climate-related objective, play a key role in this context. These climate cooperative initiatives (CCIs) can partially overcome structural barriers and limitations faced by individual FIs by fostering voluntary standards and promoting coordinated approaches. Yet, the voluntary nature of such initiatives can lead to uneven participation and limited accountability.

A more fundamental barrier lies in the broader regulatory and market environments in which FIs operate. Current incentive structures favour short-term returns and risk minimisation over long-term sustainability outcomes (Clark, Reed and Sunderland, 2018; DePillis, 2024). Climate-related risks are still poorly priced, and there are few legal or market signals that push FIs to shift capital at the pace required for Paris alignment. Without meaningful regulatory intervention to rebalance incentives and mandate Paris-aligned behaviour, even the most ambitious financial actors will struggle to allocate capital optimally or at scale. The regulatory level **(see → Chp. 4)** is therefore essential in creating an enabling regulatory and market environment.

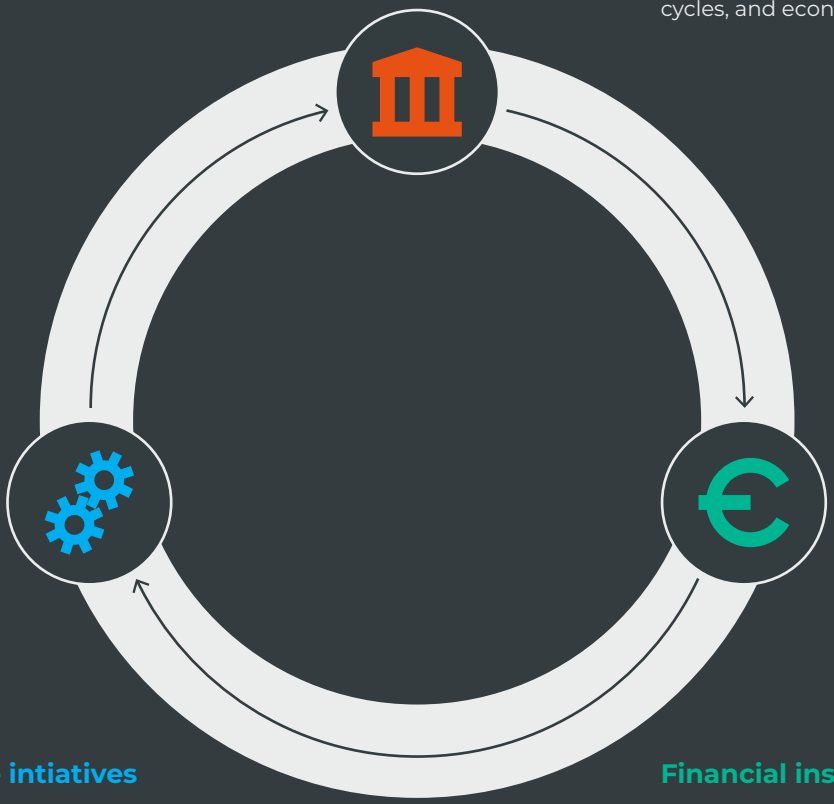
Fig. 1

The interconnections between actors governing the alignment of private finance with climate goals

Regulation

Power: Enforce policies and align frameworks to incentivise climate finance

Barrier: Anti-climate lobbying, political cycles, and economic stability concerns



Climate cooperative intiatives

Power: Overcome first-mover hesitation and pooling resources

Barrier: Voluntary nature and unequal levels of participation

Financial institutions

Power: Allocate capital and manage risks

Barrier: Fiduciary duties, resource limitations, and regulatory gaps

IMPACT LEVER FRAMEWORK

For each level, we have drawn on academic and grey literature, as well as real-world examples, to identify the factors that constrain actors in fulfilling their governance functions effectively and in alignment with the Paris Agreement. Based on this analysis, we propose, where possible, a set of impact levers, defined as key areas of influence and functions through which entities at each level can either generate impact or overcome barriers to doing so. For each impact lever, we identify a set of promising practices that can enhance its effectiveness. Taken together, these components form a framework for the governance chain of climate action within the financial sector.

To the best of our knowledge, this framework represents a novel approach by bringing together a constructive perspective on how different actors in the financial sector can exercise climate-focused governance effectively, while also emphasising their interdependence in making the overall governance chain function. However, it is important to note that the framework does not claim to be exhaustive. In particular, the regulatory level remains an area where evidence on effective impact levers and promising practices are still emerging. The defining feature at this level is often the absence of necessary regulatory intervention. Further research is therefore required to strengthen in particular this part of the framework.

/ ∧ 02

THE ROLE OF INDIVIDUAL FIs IN FINANCING THE DECARBONISATION OF THE REAL ECONOMY

FIs, including banks and asset managers, are accountable for the emissions of the real-economy assets they finance or facilitate (scope 3, category 15 emissions). However, they **lack direct managerial control** over these assets, which severely limits their ability to enforce emissions reductions or mandate change (Kachi and Marquardt, 2022). Their influence is largely indirect and mediated through capital allocation, corporate engagement, and systemic advocacy, all of which depend on the strength of their financial leverage and the willingness or capacity of investees to adapt.

Even where leverage exists, **exercising climate influence comes at a cost**. High-impact actions, such as intensive shareholder engagement and stewardship, require dedicated resources, expertise, and sustained effort, often without a clear or immediate return. In addition, **market signals and regulatory frameworks do not yet reward meaningful climate action.** Financial performance continues to be benchmarked against short-term returns, leaving little incentive for FIs to prioritise longer-term climate outcomes (Clark, Reed and Sunderland, 2018; DePillis, 2024).

In response to growing societal pressure, it is becoming increasingly common for FIs to put forward net-zero portfolio targets. However, **net-zero portfolio targets often emphasise long-term alignment over near-term impact**, and many remain disconnected from actual decarbonisation in the real economy. As a result, such commitments risk becoming symbolic gestures. To date, they have shown limited evidence of driving real change and have drawn increasing criticism for vague assumptions, lack of transparency, and minimal accountability (Lütkehermöller, Marquardt and Kachi, 2023; Sachs, Mardirossian and Toledano, 2023; Stockholm Environment Institute, 2024).

This chapter analyses the structural barriers that limit climate action of FIs in more detail and introduces a framework of impact levers, operational and strategic mechanisms through which FIs can leverage their power more credibly, even in the presence of systemic limitations. As presented in → **Tab. 1**, these levers aim not only to offer a practical toolbox, but to identify mechanisms most capable of overcoming underlying constraints and help shift financial decision-making toward real-economy decarbonisation.

Tab. 1
FI impact levers

#	Impact lever	Reasoning	#	Promising practices
1	**Engagement with credible escalation** ↗	Engagement enables FIs to put pressure on their investees or clients to transition to Paris-aligned business models. This involves engaging investees to adopt and comply with credible transition plans and setting clear escalation measures if they fail to meet climate expectations.	**a**	Clear, time-bound engagement policies and escalation strategies across all asset classes.
			b	Transparent reporting on engagement progress and outcomes.
			c	Dedicated internal resources to support engagement efforts.
2	**Exclusionary policies** ↗	FIs can indirectly influence emissions reduction in the real economy by restricting capital flow and increasing the cost of capital for certain companies. Exclusion and denial of re-entry in the primary debt and equity market can be particularly impactful.	**a**	Development of comprehensive and stringent exclusion policies with Paris-aligned timelines.
			b	Consistency across asset classes and market timing.
3	**Sustainable finance** ↗	Private sector capital is required to close the funding gap for a Paris-aligned global transition. Through increasing the share of green and transition finance as part of their portfolios, FIs can proactively channel capital towards closing this funding gap.	**a**	Transparent reporting of green finance and transition finance.
			b	Sustainable finance as the default.
4	**Systemic Intervention** ↗	To enable widespread FI climate action, FIs must support removing barriers in current legal and market systems. FIs can influence government policy and industry standards in favour of climate action directly by lobbying, and indirectly by joining a climate cooperative initiative.	**a**	Lobbying for policy and regulatory changes at the sectoral and policy levels.
			b	Improved transparency in lobbying efforts.
			c	Ceasing direct and indirect anti-climate lobbying.
			d	Proactive participation in high-integrity climate cooperative initiatives (CCIs).

LEVER 1: ENGAGEMENT WITH CREDIBLE ESCALATION

Engagement and active stewardship with clients and investees is one of the most important tools for FIs to drive real economy emissions reductions (Lütkehermöller et al., 2020; Kachi and Marquardt, 2022; NZAOA, 2024). FIs can exercise their influence through direct communication with company management and their voting power as shareholders. The impact of engagement is generally stronger when FIs hold larger ownership stakes, as this increases their access to company management and ability to drive governance reforms. For engagement to be effective, FIs must have a clear strategy with defined goals, timelines, and consequences. Including a credible escalation strategy, such as the threat of divestment or exclusion from refinancing, strengthens engagement leverage (Hoepner and Schneider, 2022; Kachi and Marquardt, 2022; Reclaim Finance, 2023a; NZAOA, 2024) **(see → FI Lever 2)**.

While engagement practices are more formalised in equity markets, engagement is less structured in fixed income markets. Bondholders have no voting rights, and there are no annual general meetings (AGMs) for direct dialogue with company management. To maximise influence, FIs should engage with issuers before new bond offerings (pre-issuance), setting clear expectations through roadshows or management meetings (Philips, 2020; Hoepner and Schneider, 2022). Frequent bond issuances and shorter maturities enhance investor leverage by providing regular opportunities to influence terms or withhold renewals if expectations are not met (Sjöstrom and Erlandsson, 2020). During the holding period, investors can maintain pressure through private dialogues, intermediaries, or collective bondholder meetings, especially during refinancing events where they can introduce new clauses or apply sanctions (Reclaim Finance, 2023a).

Several barriers limit the effectiveness of corporate engagement. Engagement is resource-intensive, making it challenging for FIs, especially smaller ones, to engage across their entire portfolios (Wu, Margolin and McGinnis, 2021). While many asset managers have ESG and sustainability teams, nearly half of those surveyed by Redington (2023) lack dedicated staff for stewardship. Hiring in these roles has also slowed and they are vulnerable to budget cuts. Even major asset managers like BlackRock and Vanguard have fewer than 50 team members dedicated to stewardship, and they are responsible for engaging thousands of companies and voting on tens of thousands of proposals (Rose, Buckley and Brown, 2021).

Additionally, engagement often occurs informally, making it difficult to track its approach, frequency, or impact. Even when engagement is successful, it is challenging to empirically capture and verify the outcomes, leading to uncertainty about actual emission reduction impacts (Kachi and Marquardt, 2022). This lack of transparency together with an apparent inconsistency between commitments and actions (Lütkehermöller, Marquardt and Kachi, 2023) weakens shareholder activism, limiting progress on emissions reductions while allowing greenwashing.

The following promising practices outline how FIs can strengthen their engagement strategies through the credible threat of escalation, adequate resourcing, and transparent reporting. These practices are exemplified in → **Box 1**, which showcases how select asset managers are beginning to implement this lever in practice.

1a. Clear, time-bound engagement policies and escalation strategies across all asset classes:

FIs could implement well-defined engagement strategies with specific goals, general and sectoral demands, timelines, and actionable steps aligned with their own climate transition plans. This includes engaging with investee companies to disclose emissions, assess climate risks, and implement robust transition plans with ambitious decarbonisation targets (NGFS, 2023b; Reclaim Finance, 2023a). To maximise impact, engagement could focus on companies with the highest current and future greenhouse gas emissions

across all scopes and sectors, such as oil and gas, coal mining, and 'hard-to-abate' sectors. Engagement policies could also include credible escalation procedures, with information like timelines, triggers, and consequences for non-compliance. The escalation toolkit would include public statements, letters to executives, votes against management resolutions, filing shareholder resolutions, divesting holdings with or without public announcement, or litigation (ShareAction, 2023a; ShareAction, 2024).

1b. Transparent reporting on engagement progress and outcomes:

Regular and transparent reporting of climate engagement progress is essential for accountability (ShareAction, 2024). FIs could publish a comprehensive stewardship report detailing engagement policies, thematic priorities, a list of companies engaged, and quantitative outcomes. A voting policy should also be made public, outlining guidelines for voting on material issues such as climate and biodiversity. Voting records should be disclosed at least annually, along with rationales for significant votes or abstentions. FIs could also vote in favour of responsible investment-related shareholder resolutions by default, using a 'comply or explain' approach. Where legally permissible, pre-declaring voting intentions on key resolutions sends a strong public signal and sets clear expectations for investees (ShareAction, 2024).

1c. Mobilisation of internal resources to support engagement efforts:

Effective engagement requires sufficient financial, human, and technological resources at all organisational levels. The appropriate number of stewardship personnel depends on the FI's type, size, the nature of their investments, and their stewardship approach. In banks, relationship managers, supported by risk and product specialists, are usually the focal point in implementing the engagement policy (Waslander, Bos and Wu, 2021). In asset managers or owners, the responsibility typically lies with the stewardship team. FIs can also supplement their in-house teams with third-party providers for services such as voting instructions, proxy research, and voting recommendations (The Investment Association, 2018), although this may carry its own limitations.

Box 1

Engagement with credible escalation lever in practice

To identify FIs demonstrating **engagement with credible escalation strategies (1a)**, we reviewed assessments from (ShareAction, 2022, 2023b, 2023c, 2023d; LobbyMap, 2023). Robeco, a Dutch asset manager overseeing EUR 180 billion in AUM (as of end-2023), consistently ranks among the top performers of these assessments. Robeco reports that EUR 143 billion of its portfolio is under engagement (not limited to climate), and EUR 76 billion is actively voted (Azizuddin, 2024). Robeco's engagement approach includes a clear, time-bound strategy guided by a 'climate traffic light' model that categorises investees as aligned, aligning, partially aligning, or misaligned with Paris Agreement goals. This model prioritises companies in high-emitting sectors such as oil and gas, electric utilities, steel, and cement, and also includes banks given their role in financing these sectors. In 2023, Robeco conducted 54 climate-engagement cases, emphasising enhanced engagement for companies it deems climate laggards, with dialogue periods set to three to four years. In 2024, Robeco imposed additional requirements on its top 250 emitters to include disclosing and setting scope 1 and 2 emissions targets, establishing methane reduction targets (for upstream oil and gas), and creating a coal phase-out plan for companies operating coal power plants above 300 MW (Robeco, 2024c, 2024a).

Escalation strategies among leading asset managers (including Robeco) typically follow progression pathways and range from sending formal letters to the CEO and publicly expressing concerns, to voting against boards' recommendations and submitting shareholder resolutions. 'Divestment if necessary' is typically regarded as a last resort after multiple years of unproductive engagement, reflecting the highest form of escalation. In a recent example, Robeco, SEB, Nordea, Achmea, PME, and Lærernes Pension jointly divested POSCO. The divestment decision was multifaceted and triggered by multiple issues beyond climate, not only failure to outline a coal phase-out plan, but also alleged deforestation, water source degradation, community displacement, military junta involvement in Myanmar, and alleged embezzlement by the incumbent chair (Azizuddin, 2024). Divestment used as a form of escalation such as in this case, however, remains scarce. To the best of our knowledge, no asset manager has initiated legal proceedings to enforce climate goals, presumably due to cost and complexity.

On a more positive note, **transparent engagement reporting (1b)** is becoming increasingly common among leading asset managers. Many now publish detailed engagement policies and plans, as well as proxy voting guidelines, along with quarterly and annual engagement reports; Robeco and Federated Hermes are notable examples. These reports typically present company-level statistics, engagement highlights, outcomes, and planned next steps. Aviva Investors and Robeco also release both their voting policies and voting history, which allows external stakeholders to understand their voting decisions and hold them accountable (Aviva Investors, 2025; Robeco, 2025). Another promising practice is pre-declaring voting intentions, as demonstrated by Legal & General Investment Management (LGIM), which publicly discloses its voting plans and rationales ahead of key shareholder meetings, forming part of LGIM's broader engagement and escalation strategies (LGIM, 2024).

However, gaps remain in terms of disclosing **internal resources and capacity allocated for engagement (1c)** since only a limited number of asset managers provide details about the structure and expertise of their engagement teams, such as Federated Hermes. Such transparency is crucial for evaluating whether FIs are dedicating sufficient resources and expertise to their engagement efforts.

LEVER 2: EXCLUSIONARY POLICIES

Exclusion, also known as negative or exclusionary screening, refers to investors deliberately choosing to exclude certain companies from their investment universe, either to reduce exposure to sectors deemed risky or harmful, or especially when engagement is unlikely to bring meaningful change or alter a company's core business model (Boffo and Patalano, 2020). Denial of re-entry, a form of timed exclusion, involves withholding refinancing from companies whose activities do not align with investor goals, leveraging influence over maturing bond debt (Hoepner and Schneider, 2022). Divestment describes the act of selling equity shares of investee companies in secondary markets. The key mechanism through which exclusion, denial of re-entry, and divestment may affect the real economy is by restricting capital flow to targeted companies. In theory, this can raise the cost of capital for excluded or denied companies and send a market signal about the undesirability of their practices (Caldecott et al., 2022).

The scope, sectoral coverage, and rigour of exclusion policies vary widely. Kachi and Marquardt (2022) found that while half of the largest 50 asset managers have exclusion policies targeting emissions-intensive sectors, most of the top 50 asset owners lack clear exclusion policies. Less than half of these asset managers limit financing for thermal coal production and coal-fired power generation, and even fewer have restrictions for oil, gas, or deforestation-linked activities. Policies often apply only to actively managed assets, leaving out passively managed funds. Some policies also only exclude project financing and not general balance sheet financing. Moreover, the effectiveness of exclusion ultimately depends on the revenue thresholds set; high thresholds allow continued financing for carbon-intensive activities, rendering the policies ineffective.

Exclusionary policies have different impacts depending on asset class and market timing (Kachi and Marquardt, 2022). Especially in fixed income markets which tend to be less liquid, exclusion policies can notably reduce the pool of investors. This forces companies to offer higher interest rates on bonds, which makes fundraising and debt refinancing more expensive. This particularly affects capital-intensive sectors like fossil fuels, which regularly raise debt capital through loans and bonds for primary financing and working capital (Cojoianu et al., 2019). In primary equity markets (e.g. initial public offerings), exclusion can also lower valuations as reduced demand drives down share prices, limiting companies' ability to raise capital for new projects or expansion (Kachi and Marquardt, 2022). The low frequency of initial public offerings, however, limits the impact potential for exclusion in equity markets.

Exclusion and divestment in secondary equity markets have only a limited direct impact on a company's finances or emissions, as they do not affect cash flow but remove the investor's ability to engage with the company. Focusing on portfolio decarbonisation has led to 'paper decarbonisation', where portfolios appear to

meet climate goals on paper, but the actual impact on emissions in the real-world is minimal or even counterproductive (Caldecott, 2024). While some divestment campaigns may create reputational damage or stigmatisation that could indirectly increase borrowing costs, this effect is generally limited by market liquidity and the availability of neutral investors who step in to stabilise stock prices (Ansar, Caldecott and Tilbury, 2013; Berk and Binsbergen, 2021).

The following promising practices provide guidance on how FIs can strengthen the design and implementation of exclusionary policies to maximise their real-economy impact and minimise loopholes. These approaches respond to the limitations discussed above and are further illustrated through practical examples in → **Box 2**, which highlights how certain FIs are beginning to operationalise exclusionary policies, while shedding light on the broader gaps that remain across the sector.

2a. Development of comprehensive and stringent exclusion policies with Paris-aligned timelines:

Exclusion policies should prioritise high-emitting sectors, such as conventional and unconventional fossil fuels and deforestation-linked commodities (e.g. beef, palm oil, soy). These exclusions should span the entire value chain, from extraction and processing to transportation and distribution, and include measurable criteria such as revenue or production thresholds (Reclaim Finance, 2023b, 2023c, 2023d). To avoid loopholes, policies should also apply to both corporate and project-specific financing. FIs could align exclusion timelines with science-based deadlines established by credible organisations such as the UN High-Level Expert Group (UN HLEG, 2022). Transparency is also critical: FIs could regularly disclose and update their exclusion criteria and the list of covered entities.

2b. Consistency across asset classes and market timing:

Exclusion policies must be consistently applied across all asset classes (including public and private equity, corporate and sovereign debt) to prevent companies from bypassing restrictions through less-regulated funding channels. Market timing plays a crucial role in amplifying the impact of exclusion policies. Exclusions are particularly powerful during capital-raising events, such as initial public offerings (IPOs) and bond issuances, when companies are actively seeking funds for new investments (Kachi and Marquardt, 2022).

Box 2

Exclusion, denial of re-entry, and divestment lever in practice

Based on Reclaim Finance's Coal Policy Tracker (2025a) and Reclaim Finance's Oil and Gas Policy Tracker (2025b), La Banque Postale offers a promising example of how FIs can **develop comprehensive and stringent exclusion policies with Paris-aligned timelines (2a)**. It is among the world's first banks to commit to fully exiting both conventional and unconventional oil and gas, covering shale oil and gas, deepwater operations, tar sands, and Arctic drilling, as well as thermal coal, by 2030. The bank references the Global Oil and Gas Exit List (GOGEL) and the Global Coal Exit List (GCEL) databases to guide its policies, which cover upstream and midstream activities, prohibit financial services for companies expanding oil and gas operations through new exploration or infrastructure projects, and require gradual divestment from entities engaged in lobbying for oil and gas. Under these guidelines, La Banque Postale maintains relationships only with companies that have credible, public strategies to exit oil and gas by 2040 and coal by 2030, provided they refrain from any new fossil fuel projects beyond 2030 and direct financing exclusively toward renewable energies or sustainable fuels. The bank also strongly encourages closing, rather than selling, coal assets and will discontinue support for organisations lobbying to delay or block a 2030 coal phase-out (La Banque Postale, 2023b, 2023a). At the end of 2023, the bank reported nearly achieving its goal, with only 0.01% net exposure remaining (La Banque Postale, 2024). Despite setting this precedent, it is worth noting that La Banque Postale's initial exposure to fossil fuels was relatively low (around 2%), potentially making it easier to meet its targets (Furness, 2021).

The vast majority of FIs still maintain far less stringent exclusion policies. Many continue to finance fossil fuel companies without clear restrictions on conventional oil and gas. Even where exclusion policies exist, they often have a limited scope and fail to address the core drivers of emissions, leaving a major gap in efforts. Moreover, transparency and accountability remain inconsistent across the sector, making it difficult to assess the real-world impact of many exclusion claims, including whether **exclusion policies are consistently applied across all asset classes and at the right market timing (2b)**.

LEVER 3: SUSTAINABLE FINANCE

The mobilisation of private sector capital is critical to addressing the transition financing gap (Mohieldin and Fulga, 2024). FIs can tilt their portfolios towards more meaningful inclusion of sustainable finance, for example through better integration of ESG factors into financial decision making, or more actively by directing capital towards green and transition activities. Green finance refers to investments or lending aimed at activities that are already considered environmentally sustainable. In contrast, transition finance supports activities that are not yet sustainable but are on credible pathways towards environmental improvement.

The financial sector continues to face challenges in defining and reporting green and transition finance in a consistent manner. Specifically for the latter, scientifically robust definitions are only beginning to emerge. Financial regulators remain insufficiently equipped to enforce accurate reporting and to address concerns related to greenwashing and transition-washing at scale (Lombos, 2024). Greenwashing involves overstating the sustainability of investments that are not genuinely green. Transition-washing refers to financing carbon-intensive assets without credible evidence of progress towards sustainability. Resulting ambiguity undermines market integrity and investor confidence, potentially leading to a misallocation of capital and delaying genuine progress towards net-zero goals (Lombos, 2024), and introduces micro and macro-financial stability risks (Bingler et al., 2023).

Financial institutions tend to allocate insufficient capital to green and transition activities. Climate-related risks remain poorly priced in financial markets, and most institutions have yet to interpret their fiduciary duties as requiring the integration of such risks. While progress has been made in some jurisdictions (most notably the European Union with its Sustainable Finance Disclosure Regulation (SFDR)), where regulation now requires at least the disclosure of sustainability risks as part of fiduciary responsibilities, these remain exceptions rather than the rule and do not necessarily result in more sustainable finance.

On the supply side, a shortage of bankable projects and credible financial instruments, particularly in areas such as transition finance where definitions and metrics remain contested, raises transaction costs and further weakens the risk-return profile of these finance types (Harnett, et al., 2024; Winnie and Vinelli, 2024). Currently, the most convincing developments are in fixed income markets, where labelled instruments such as green, sustainability, and climate bonds have gained traction, offering a broad range of investors access to green and transition finance at market rates. These markets continue to grow and are supported by well-established standards. In public equity markets, ESG-themed investing is already widespread, though the absence of consistent and robust standards still undermines the credibility of ESG classifications. Transition equity finance, which remains more complex to define and regulate, has so far emerged mainly in private markets, specifically through climate tech-focused venture capital (OECD, 2022). Requiring investee companies to publish credible transition plans will be essential to help equity and fixed income investors assess and track the effectiveness of transition finance.

Private financial institutions, given their finance-first mandates, cannot be expected to finance the transition on their own. Many of the necessary investments target technologies or sectors that are not yet commercially viable and will not attract private capital without public support in the form of regulatory frameworks and market incentives **(see → Chp. 4)**. However, financial institutions have significant

potential to enhance the impact of their portfolios by promoting greater transparency and by adopting a forward-looking interpretation of fiduciary duties that shifts investment focus to sustainable finance.

The following promising practices outline how FIs can mobilise more capital for a Paris-aligned transition while mitigating greenwashing and transition washing risks. These practices are illustrated through examples in → **Box 3**, which showcases early implementation efforts by certain FIs, while highlighting the broader challenges that persist in mainstreaming sustainable finance.

3a. Transparent reporting on green and transition finance:

To prevent greenwashing, transition washing or impact washing, FIs could apply recognised frameworks when reporting on sustainable finance and impact investing. The EU's Sustainable Finance Taxonomy, the UK Green Taxonomy, as well as Canada's Green & Transition Taxonomy are examples of public frameworks set to classify mostly green and some transition activities. The Climate Bands Initiative (CBI) Taxonomy and ICMA's Green Bond Principles (GBP), as well as ISO's 14030-3:2022 Green Taxonomy standard, are established private sector examples of guidelines and frameworks for green finance. For transition finance, private frameworks have also started to emerge recently, such as GFANZ's Transition Finance Framework, ICMA's Climate Transition Finance Handbook, or CBI's Framework to Assess Transitions.

3b. Sustainable finance as the default:

FIs could increase the share of green assets and assets managed in line with sustainability principles within their portfolios. At a minimum, this requires comprehensive negative ESG screening to ensure portfolios are not exposed to carbon risks, as well as positive ESG screening and thematic investment strategies to actively channel capital towards green and transition-related investments. FIs can access established green finance instruments on both fixed income markets and equity markets, but need to be cautious to use credible standards and taxonomies (see above). When it comes to transition finance, investors could place greater focus on the transition plans of investee companies and link investment decisions to the credibility of these plans. To scale up green and transition finance, public support may be required, including mechanisms such as blended finance, to reduce investment risks and improve the risk-return profile of such assets (Mak, Winnie; Vinelli, 2024).

Box 3

Sustainable finance lever in practice

Progress on more transparent and **robust reporting of green and transition finance (3a)** is slow. Greenwashing and transition washing remain difficult to detect but are increasingly recognised as widespread issues (Reuters, 2023). In 2025, the German asset manager DWS was fined €25 million by the US SEC for misleading claims, including portraying ESG as 'an integral part' of its business model (Segal, 2025). The commercial appeal of sustainability claims, combined with the complexity of financial products, facilitates both green and transition washing. This complexity stems not only from ambiguity around what qualifies as green or transitional activities but also from the intricate structure of funds and investment products, which obscures the actual sustainability profile of the underlying assets. Regulations such as the EU's Sustainable Finance Disclosure Regulation (SFDR), and equivalent efforts in the UK and US, aim to standardise fund labelling, but implementation challenges persist. Despite SFDR classifications, including Article 8 (funds promoting environmental or social characteristics) and Article 9 (funds with sustainable investment as an objective), 'green' funds in Europe were still found to hold over USD 33 billion in oil and gas investments (Carrington, Michalopoulos and Valentino, 2025).

While ESG-managed and **sustainable finance are not yet the default (3b)**, they are expanding. In the US, 12% of total assets under management in 2024 were classified as ESG or sustainable, although much of this remains concentrated in strategies based on negative screening rather than thematic or impact-oriented investment (US SIF, 2024). Still, investor interest in more impactful solutions is growing. In the EU, the share of sustainably managed assets is significantly higher, around 38% in 2024, largely due to the regulatory framework for sustainable finance (EPRS, 2024). Transition finance is also gaining traction, particularly in Europe, though the absence of clear definitions and regulatory safeguards continues to hamper its full potential (Better Finance, 2024).

Some FIs have taken more credible steps by offering investment vehicles that explicitly support the low-carbon transition. ABN Amro's Sustainable Impact Fund aims to invest EUR 1 billion by 2030 in early-stage capital for decarbonising the construction, food, and textile sectors, using a mix of equity, external funds, and hybrid loans (ABN AMRO, 2023). HSBC has partnered with Google to provide USD 1 billion in flexible venture debt for climate technology firms focused on energy transition, transport electrification, supply chain sustainability, and climate resilience (Jessop and Cruise, 2024). Blended finance instruments have further potential to mobilise capital in areas underserved by private investment. The SDG Loan Fund, managed by Allianz Global Investors and supported by FMO and a USD 25 million guarantee from the MacArthur Foundation, has mobilised USD 1.1 billion to advance the SDGs in emerging markets (Higgins, 2024). It targets affordable energy, financial inclusion, and sustainable agriculture across Latin America, Asia, Africa, and Eastern Europe.

LEVER 4: SYSTEMIC INTERVENTION

Systemic intervention refers to an individual FI's capacity to engage with and influence the broader systems in which it operates, addressing sectoral and policy-level barriers that can limit climate action within the financial sector (Hafner et al., 2020; Bhat et al., 2023). This is essential as current legal and economic systems still fail to incentivise, and may even hinder, FIs in aligning their decision-making with climate objectives **(see → FI Levers 1-3)**. By engaging proactively with stakeholders both within and beyond their immediate scope, FIs have the potential to drive meaningful, systemic change (Micale et al., 2024). However, the potential is largely underutilised, and multiple challenges hinder the effectiveness of these interventions.

FIs show limited strategic engagement with sustainable finance policy, generally only issuing broad, high-level statements rather than having direct involvement in influencing government policy (InfluenceMap, 2022a). Furthermore, while banks may conduct climate-focused multi-level engagement activities with different stakeholders, these efforts are frequently uncoordinated. For example, aviation and regulatory affairs teams within the same institution may independently advocate for sustainable fuel standards upgrades to the policymakers (Bhat et al., 2023).

Another main issue is the disconnect between FIs' climate commitments and lobbying activities. Despite their positive public messaging on climate action, many FIs maintain memberships and even hold influential roles in industry associations that obstruct climate policies or lobby for fossil fuel interests (InfluenceMap, 2022a, 2023). Despite being more vulnerable to climate transition risks than smaller or less exposed institutions, larger and more leveraged financial institutions are often found lobbying against stricter climate policies (Hawser, 2024). Almost a third of the institutions assessed by InfluenceMap (2022a) are members of real-economy industry associations that have directly lobbied in favour of fossil fuel interests, like the US Chamber of Commerce and the American Bankers Association. For example, the US Chamber of Commerce extensively lobbied against the USD 3.5 trillion Inflation Reduction Act (also known as the 'Build Back Better' bill) in 2021, ultimately leading to the scaling back or elimination of critical climate elements (InfluenceMap, 2023). While the American Bankers Association advocated against climate-related financial risk management policies, arguing that it was 'premature' and 'too prescriptive' (InfluenceMap, 2023).

Adding to the challenge is the lack of transparency in these lobbying efforts, much of which occurs behind closed doors. While some forms of lobbying, such as regulatory consultation comments, are publicly accessible, they represent only the tip of the iceberg. Many other activities remain opaque, including political donations, private meetings, and potentially illegal actions like bribery or corruption (InfluenceMap,

2021). There is far less visibility into lobbying efforts aimed at weakening or delaying pro-climate policies. For instance, J.P. Morgan, one of the biggest financiers of oil and gas, reportedly lobbied extensively in 2021 against the Climate Change Financial Risk Act, a bill that would have introduced mandatory climate risk stress tests for major FIs (Bindman, 2022).

Out of the 30 institutions assessed by InfluenceMap (2022a), none of the FIs meet lobbying transparency expectations as outlined by initiatives like Principles for Responsible Investment (PRI), The Institutional Investors Group on Climate Change (IIGCC), and Ceres Investor Network. Among those, several FIs disclose no information on their industry association memberships, while others list memberships without detailing the associations' activities or alignment with the institutions' sustainable finance goals. Only a few offer limited additional information, such as board memberships, but still omit key details on policy positions and alignment on critical sustainability issues.

The following promising practices outline how individual FIs can leverage their influence to drive systemic change at the policy and sectoral levels. These practices address the key challenges identified above and are further illustrated through real-world examples in → **Box 4**, which demonstrates how some leading FIs have begun to put these interventions into action.

4a. Lobbying for policy and regulatory changes at the sectoral and policy levels

Individual FIs could actively support policy changes at both the sectoral and policy levels to eliminate barriers to individual or collective climate action. Sector-level engagement involves collaborating with academic institutions, civil society, and trade associations, for instance, to establish common emissions disclosure metrics and sector-wide decarbonisation pathways (Bhat et al., 2023). At the policy level, FIs could advocate for stronger government policies and push for new legal obligations that require companies to rapidly decarbonise. FIs could also promote the transition from voluntary pledges to enforceable regulation, leveraging the 'conveyor belt' mechanism to strengthen accountability, transparency, and market integrity (Hale, 2022; Caldecott, 2024). Coordination of engagement efforts can work by bringing together internal stakeholders and creating engagement mapping tools that align shared goals and prioritise actions (Bhat et al., 2023).

4b. Improved transparency in lobbying efforts

FIs could prepare comprehensive reports on direct and indirect lobbying activities. This includes disclosing lobbying efforts, expenditures, and industry association memberships, as well as supporting shareholder resolutions that call for transparency and Paris alignment. Ideally, the reports should follow the policy advocacy and transparency framework as outlined by initiatives like

Principles for Responsible Investment (PRI), the Institutional Investors Group on Climate Change (IIGCC), and Ceres Investor Network (PRI and IIGCC, no date; PRI, 2018). Enhanced transparency enables stakeholders to assess the alignment between lobbying activities and sustainability objectives, fostering accountability and trust.

4c. Ceasing direct and indirect anti-climate lobbying

FIs could limit and eventually eliminate their memberships in associations that obstruct climate policies. They could reconsider affiliations with groups directly linked to fossil fuel support activities, such as the Canadian Association of Petroleum Producers, and industry associations such as the US Chamber of Commerce, European Issuers, and Business Europe, which have historically lobbied against sustainable finance policies and environmental regulations (InfluenceMap, 2022a). Aligning policy advocacy efforts with climate targets enhances credibility and reduces the risk of greenwashing.

4d. Proactive participation in high-integrity climate cooperative initiatives (CCIs)

Participating in CCIs that progressively push for the system towards higher integrity climate action enables financial institutions to collectively shape sector standards and advocate for climate-aligned financial policies, creating commercial pressure for behavioural change. Individual entities can amplify their influence through coalition membership, leveraging shared platforms to drive systemic change. Members of such coalitions are significantly more likely to set climate targets and take action, suggesting a strong link between coalition participation and climate ambition, although the causality may be bidirectional (Micale et al., 2024). For further discussion on the determinants of promising CCIs, refer to → **Chp. 3**.

Box 4

Systemic intervention lever in practice

A selected review of FIs ranking highest on **policy engagement (4a)** (LobbyMap, 2020, 2023; InfluenceMap, 2022a; ShareAction, 2023b) showed that leading FIs are actively advocating for climate policy. For instance, Aviva issues policy position papers advocating for mandatory climate disclosures and net-zero mandates, while Triodos Bank supports EU-wide reforms (e.g. stronger SFDR and CSDDD) and participates in a fossil fuel non-proliferation campaign. Legal & General Investment Management similarly calls for stricter climate and biodiversity regulations, opposing new legislation in the US and UK that undermines ESG integration. Another noteworthy move is a group of 25 investors coordinated by PRI, who conducted targeted sovereign engagement to influence the formulation of Australia's 2035 NDC targets, advocating for greater ambition based on the rationale that national policy commitments are the key to guiding companies in setting their climate transition plans (PRI, 2024; Robeco, 2024b).

While high-level advocacy is growing, targeted efforts to shape sectoral policy remain uncommon. Emerging examples include Société Générale and Citi, which demonstrate promising practice by taking leading roles across sector-specific initiatives like shipping (The Poseidon Principles), aviation (The Pegasus Guidelines), steel (Sustainable Steel Principles), and aluminium (Sustainable Aluminium Finance Framework) through working groups in the Center for Paris-aligned Finance facilitated by RMI (RMI, 2022b, 2022a; Societe Generale, 2022, 2024).

Progress on **lobbying transparency (4b)** remains limited. In the US, the Lobbying Disclosure Act obliges American FIs to report their lobbying activities, political donations, administrative support to Political Action Committees, lobbying-related expenditures, and trade association memberships. The EU and UK lack a comparable binding mandate, resulting in mostly voluntary disclosures by European and British institutions. This gap may be partly due to the differing political environments: the US operates under a high-stakes, 'winner-takes-all' system with frequent elections, creating strong incentives for aggressive lobbying, while the EU's more technocratic, consensus-driven approach creates less urgency and fewer incentives for such activity (Mestey-Colon, 2024). Nevertheless, independent assessments, such as those by InfluenceMap (2022a), enable more systematic tracking of FIs' lobbying efforts and help **identify anti-climate lobbying activities (4c)**. For further discussion on **participation in high-integrity CCIs (4d)**, refer to → **Chp. 3**.

/ ∧ 03

THE ROLE OF CCIS IN SCALING VOLUNTARY ACTION FOR REAL ECONOMY

Numerous Climate Cooperative Initiatives (CCIs) have been launched to address some of the key barriers that limit the impact potential of FIs' climate action (Stockholm Environment Institute, 2024). These initiatives work to align financial practices with climate goals by encouraging FIs to adopt goals and strategies that increase climate-related decision-making (Chan et al., 2022). By fostering collaboration, promoting shared standards, and facilitating learning, CCIs can help address structural challenges faced by FIs, such as limited leverage due to the lack of direct managerial control, the high transaction and engagement costs associated with meaningful climate action, and the absence of market signals or regulatory frameworks that reward Paris-aligned investment decisions (Chan et al., 2022).

The effectiveness of CCIs in achieving real-economy outcomes is currently constrained by several barriers. First, many CCIs **focus on net-zero target-setting frameworks** rather than supporting operational levers at the FI level that are more likely to produce measurable reductions in financed emissions **(see → Chp. 2)**. When these target frameworks are vague or lack credibility, the disconnect between ambition and action becomes pronounced, risking the diversion of resources from where they could be used more impactfully.

Second, the **voluntary nature of CCIs** means that most lack robust accountability mechanisms. Membership typically comes without binding obligations or meaningful enforcement. This opens the door to symbolic participation and weak compliance, and places pressure on coalitions to relax criteria in order to retain or grow their membership base. This dynamic has become particularly visible in larger initiatives such as GFANZ, where efforts to maintain cohesion have come at the expense of ambition and clarity (Reclaim Finance, 2023a).

Third, the effectiveness of CCIs is heavily influenced by the **broader political and regulatory context and external pressure**. Recent developments in the United States show how quickly external pressures can erode coalition stability. In response to shifting political agendas and regulatory uncertainty, several major US-based banks and asset managers have withdrawn from initiatives like the Net Zero Banking Alliance and the Net Zero Asset Managers initiative, undermining coalition credibility and weakening momentum (Gandel, 2025; Kerber, 2025).

This chapter examines these challenges in more detail and introduces a set of impact levers designed to improve the governance and effectiveness of CCIs. These are aimed at identifying where and how CCIs can drive greater impact by providing more targeted support to FIs with a focus on achieving tangible results in the real economy.

Tab. 2
CCI impact levers

#	Impact lever	Reasoning	#	Promising practices
1	**Mobilising real world decarbonisation** ↗	To drive climate action in the real economy, CCIs could support members to adopt strategies that are most effective in driving real economy decarbonisation (outlined in Chapter 2).	**a**	Including specific action targets on real-economy decarbonisation as part of CCI commitment.
			b	Supporting FIs capacity building to implement effective engagement.
2	**Accountability mechanisms** ↗	To deter FIs from using CCI membership as greenwashing, holding member FIs accountable to their commitments is necessary (Nelemans, 2023; Liu et al., 2024). Similarly, to ensure the CCI is making choices in line with its ambition, institutional-level accountability is important. This includes effective institutional set-up and robustness to enable CCIs to reach the necessary scale, longevity and collaboration amongst various stakeholders to have meaningful climate impact (Pattberg et al., 2012; Ostrom, 2015; Widerberg and Pattberg, 2017).	**a**	Effectively leveraging soft power in holding FIs accountable to commitments.
			b	Adopting a resilient institutional framework that fosters high ambition amongst various stakeholders.
			c	Promoting external accountability through public transparency.
3	**Systemic intervention** ↗	To accelerate and not hinder climate action, the regulatory environment needs to be reformed. CCIs can lobby for regulatory change that supports this aim and require their members to do the same. If their measures (Lever 1) are proving effective (Lever 2c) they could also advocate for them to be mainstreamed through mandatory adoption.	**a**	Lobbying for climate progressive regulatory frameworks.
			b	Requiring member FIs to advocate for regulatory reform.
			c	Establishing pathways for legal adoption of voluntary measures.

LEVER 1: MOBILISING REAL-WORLD DECARBONISATION

CCIs are useful catalysts for large-scale FI climate action as they amplify demands and leverage coordinated efforts to make changes at the systems level (Bernstein and Hoffman, 2018). By guiding their signatories to adopt effective levers for impact, as outlined in → **Chp. 2**, CCIs can steer FIs to advance the decarbonisation of the real economy. Recognising that these strategies may be difficult for individual FIs to implement independently, CCIs can build capacity through guidance, resources, and platforms for collaboration among institutions (Mazzucato et al., 2021).

Despite significant investments in resources for knowledge-sharing to support the financial sector's transition toward Paris-aligned practices (Stockholm Environment Institute, 2024), most CCIs currently fail to leverage effective impact channels. Net zero or carbon neutrality targets have motivated FIs to think about climate and provided a mandate for them to act on it, however, to date, they have shown little evidence of tangible impact on emissions of real-economy assets (Sachs, Mardirossian and Toledano, 2023). As outcome targets with inconsistently defined

frameworks, they lead to the adoption of strategies with limited tangible impact, and in the worst case, leave loopholes for greenwashing (Reclaim Finance, 2023a). For instance, Atta-Darkua et al. (2023) find that both investor signatories of CDP and CA100+ predominantly shift their portfolios towards companies with lower carbon emissions, rather than conducting targeted engagement with high-emission companies, to reduce emissions. While this decarbonises a portfolio on paper, it does not decarbonise the real economy. Similarly, Hastreiter (2024) questions the efficacy of collective engagement under CA100+, highlighting that while it led to heterogeneous effects on medium- and long-term company targets, it did not have a significant effect on companies' emissions disclosure, emissions' reduction or short-term targets, key indicators of high integrity.

The following promising practices outline how CCIs can shift their focus away from replicating target-setting frameworks used in the real economy. As exemplified in → **Box 5**, these measures enhance the impact channels through which FIs can most effectively influence real economy emissions:

1a. Including specific action targets on real-economy decarbonisation as part of the CCI commitment:

CCIs could require FIs to adopt specific targets on actions that drive real-economy decarbonisation, as part of their signatory commitment, as detailed in → **Chp. 2**. Setting the expectation for specific actions, rather than outcomes that are not well defined and can be manipulated, is essential. Coordinated approaches to engagement and escalation, along with a clear focus and guidance on sustainable finance and the use of transition plans, can achieve greater impact than isolated actions by individual institutions.

1b. Supporting FIs' capacity building to implement effective engagement:

CCIs could provide capacity building support to help FIs identify and implement engagement strategies. CCIs can do this by creating platforms for FIs to share experiences, learn from each other, and tackle common challenges, such as data and knowledge gaps. While general engagement guidance is useful, it needs to be tailored to fit the specific roles and capacities of each FI. To achieve this, CCIs could collaborate directly with FIs to design customised strategies based on the institution's type, investment portfolio, and context and concentrate on the engagement that can achieve the greatest influence.

Box 5

Mobilising decarbonisation in practice

The role of **engagement as a method (1a)** to put pressure towards real economy decarbonisation is emphasised by some CCIs, although their overarching approach is still requiring FIs to set net zero targets. The NZAOA guidelines suggest that members engage in corporate and industry actions to achieve the outlined net-zero targets (NZAOA, 2024). PAAO's Net Zero Investment Framework recommends implementing a stewardship and engagement strategy, with a clear voting policy that is consistent with an objective for all assets in the portfolio to achieve net zero emissions by 2050, with additional targets for climate solutions and engagement thresholds (Paris Aligned Asset Owners, 2025a). CA100+ places a strong focus on engagement (Climate Action 100+, 2025), though its impact on real-world decarbonisation has been questioned (Hastreiter, 2024). Some CCIs are starting to require specific action targets on real-economy decarbonisation as part of their commitment. While SBTi's approach in its Financial Institutions Net-Zero Standard draft is still focused on FIs setting overarching net-zero targets, it would also require benchmark targets based on a predefined list of emission-intensive sectors that are important to the broader energy transition (SBTi, 2024). This focus on sector-specific targets represents a step toward more precise and actionable transition planning and provides a starting point for mobilising sector-specific engagement.

In terms of **tools that support engagement (1b)**, many CCIs publish general advice and do not collaborate directly with FIs to design customised strategies based on the institution's type or do not publicly describe this. Some CCIs do publish resources, but they mainly focus on target setting rather than implementing change. An example of actionable guidance is CA100+ 'Net Zero Company Benchmark' (Climate Action 100+, 2023). It offers its members and the public assessments of company performance against the initiative's objectives and overall net zero transition. These assessments, which are based on using publicly available and self-reported data, can be used by investors as the basis for strategic engagement. In conjunction with other CCIs, they have also developed thematic and sectoral engagement guidance, including on electric utilities, steel, food and beverage and aviation.

LEVER 2: ACCOUNTABILITY MECHANISMS

Trust in CCIs' ability to mobilise real-world decarbonisation is created in two ways. First, CCIs foster trust by ensuring members honour their climate commitments, preventing signatories from making hollow or symbolic pledges (Hale, 2022). Second, they maintain credibility and legitimacy by actively demonstrating progress toward their mission (Raskin and Leng, 2024). Accountability mechanisms serve as tools that enable, showcase and reinforce this trust.

Currently, CCIs struggle with enforcing participant adherence to commitments because participation is voluntary, making internal enforcement mechanisms weak (Hale, 2022). As a result, CCIs often sacrifice ambition levels, as it can deter

member participation or prompt withdrawal (Dohle, 2025). This is exemplified by the ongoing dilution of GFANZ membership criteria in response to recent member withdrawals (Marsh, 2024a; Serenelli, 2025). Gaps in capacity to oversee signatories' commitments, on the other hand, can further undermine accountability (Stockholm Environment Institute, 2024). A study on 41 investor climate initiatives found transparency and accountability to be the least implemented governance functions, whilst most resources are concentrated on furthering knowledge and learning (McDonnell, Rempel and Gupta, 2022).

The lack of enforcement of accountability is evident in FIs having joined CCIs, adopted seemingly ambitious targets, and later evaded compliance without consequences or simply withdrawn when the terms became unfavourable to them (Buller, 2025). For instance, numerous banks quit the NZBA, raising questions on the original sincerity of their commitments. Among the most notable departures were JP Morgan Chase, Citigroup, and Bank of America, three of the largest fossil fuel financiers from 2016 to 2024 (Rainforest Action Network, 2024; Dohle, 2025). In total, these institutions lent the fossil fuel sector more than a trillion dollars. These figures validate concerns that the banks' participation in climate initiatives may have been more about optics than genuine commitment.

Externally, CCIs lack transparency on their progress and challenges, limiting external scrutiny (Hucke, 2024; Wicke et al., 2024). A lack of data makes it difficult to assess their impact, which does not ensure that CCI resources, capacity and time are being effectively used, and conflicts of interest are avoided (Widerberg and Stripple, 2016; Chan et al., 2022). For example, the NZBA's latest progress report (UNEP, 2024a) highlights banks' progress on targets, but provides little detail on whether they are reducing lending to the fossil fuel industry, one of the key pillars of decarbonising the real economy. In contrast, Rickman et al. (2024), question whether NZBA signatories can achieve significant fossil fuel phase-outs.

As government action on Paris-aligned finance is lagging and even backsliding around the world (Newell, 2024), voluntary initiatives and their accountability mechanisms have an important role to play, despite their limitations. Ultimately, CCIs' accountability mechanisms cannot replace a formal governance system. This involves a clear separation of accountability and standard-setting functions across regulators and independent standard setters, which is most effective at reducing conflicts of interest (Hans et al., 2023). Nor can they substitute for a legal framework that mandates FI climate action through hard law **(see → Chp. 4)**. However, CCIs can strengthen their impact through the promising practices outlined below and illustrated in → **Box 6**:

2a. Effectively leveraging soft power in holding FIs accountable to commitments:

To prevent symbolic pledges, CCIs need robust institutional structures that can withstand external pressures, uphold pledges and attract a diverse range of FIs beyond those already committed to climate action. Accountability must be embedded within institutional structures through strong monitoring and transparency mechanisms (Kuramochi et al., 2024). This involves mandating transparency and compliance with signatory requirements from the onset and at short term interim milestones. Regular assessments by an independent review group can evaluate whether FIs are fulfilling their commitments, with anonymisation applied to reduce bias in progress evaluations. CCIs could conduct ex-ante and ex-post verification of adherence to commitments (Hans et al., 2023).

While CCIs serve a mobilising rather than punitive role, it is essential to establish a clear escalation process for persistent non-compliance to ensure the CCI retains ambition and legitimacy. This could include measures such as delisting members who fail to meet critical milestones. To enhance accountability and foster societal dialogue, removals of members could be publicly announced rather than handled discreetly. By leveraging reputational pressure, CCIs can encourage compliance and reinforce the credibility of CCIs as agents of meaningful change. A key enabler of these accountability mechanisms is robust institutional capacity, including dedicated staff and resources (Kuramochi et al., 2024).

2b. Adopting a resilient institutional framework that fosters high ambition amongst various stakeholders:

Establishing a strong institutional structure is essential to ensuring CCIs standards are free from vested interests' influence that conflict with science-based goals. A well-structured institutional framework can enhance cooperation across diverse stakeholders and drive high ambition climate initiatives (Pattberg et al., 2012; Ostrom, 2015; Widerberg and Pattberg, 2017). This includes a transparent organisational structure and secure funding (Kuramochi et al., 2024). Additionally, we identify the leadership setup and CCI focus **(see → Box 6)** as a key determinant of a resilient institutional framework. Hybrid institutional setups, which involve both state and non-state actors, provide a greater mandate to CCIs to strive for high ambition and robust practices.

CCIs DIFFERENTIATE THEMSELVES ACROSS TWO DIMENSIONS:

Focus

Some CCIs are tailored to specific types of FIs, such as the Net-Zero Banking Alliance, while others address particular challenges, like evaluating transition plans, as seen with the Transition Plan Taskforce (TPT), or validating climate targets, exemplified by the Science-Based Targets initiative. These categories are not always distinct, as some CCIs simultaneously target specific FIs and specific challenges.

Leadership model

Some CCIs are industry-led, such as Climate Action 100+, while others adopt a hybrid institutional approach that combines efforts from the private and public sectors. The TPT is an example of a hybrid model, fostering collaboration among state and non-state actors, with a state-provided mandate.

Tab. 3
Simple framework of CCI dimensions

		Leadership model	
		Industry-led *Driven primarily by private-sector entities, usually organized within specific industries.*	**Hybrid approach** *Combines voluntary efforts from both private and public sectors, fostering collaboration across stakeholdres.*
Focus	**Targeting specific FIs** *Focused on specific types of financial institutions, providing for example frameworks and guidelines for Net-Zero commitments.*	e.g. Glasgow Financial Alliance for Net-Zero alliances	e.g. Forum for Insurance Transition to Net-Zero
	Targeting specific challenges *Aimed at particular climate action challenges, such as assessing transition plans or validating targets for emissions reduction.*	e.g. Science-Based Targets initiative	e.g. Transition Plans Taskforce

2c. Promoting external accountability through public transparency:

CCIs could publish comprehensive, publicly accessible reports on their members' progress towards their engagement and real-world decarbonisation, backed up with comprehensive data and details on their achievements and challenges (Raskin and Leng, 2024). This enables independent watchdogs, like Reclaim Finance and ShareAction, to conduct regular audits to enhance transparency and public trust. A further proactive step is conducting attribution analysis on the impact of actions encouraged by CCIs, allowing them to refine strategies and promote effective practices to others (Spalding-Fecher et al., 2021).

Box 6

Accountability mechanisms in practice

Most CCIs do not fully utilise their **informational and reputational soft power (2a)** to enforce FIs' accountability. Prioritising accountability from the onset of membership, the NZAM previously specified that it had the right to reject an asset manager's request to join the initiative if there were doubts about the manager's ability or intent to comply with its commitments, or the member could undermine the initiative's credibility and reputation (NZAM, 2024). However, the NZAM is currently conducting a review of its own 'fit for purpose in the new global context', following the withdrawal of several members (NZAM, 2025). To hold members accountable to meeting targets, the SBTi publicly lists FIs that have failed to meet their targets on its dashboard as 'commitment removed' (Science Based Targets Initiative, 2023). This increased transparency ensures that unmet commitments are clearly visible, pushing FIs to uphold their climate obligations and reinforcing the credibility of SBTi. Similarly, CA100+ has taken steps toward greater transparency by publicly addressing recent member departures and explaining the circumstances surrounding them (Climate Action 100+, 2024). While NZBA and NZAOA feature the members that are no longer part of their Alliance, they are not featured prominently and require scrolling to the bottom of the webpage (NZAOA, 2025; NZBA, 2025).

An example of adopting **an institutional framework (2b)** that fosters collaboration amongst various stakeholders and is more resilient to legal pressures is the Forum for Insurance Transition to Net Zero (FIT) successor to the Net-Zero Insurance Alliance (UNEP, 2024b). Although FIT imposes weaker requirements by not mandating interim decarbonisation targets for insurance underwriting portfolios, it incorporates key lessons from the shortcomings of NZIA (Marsh, 2024b). This includes establishing a legal team of antitrust and competition law experts and offering expert support to help insurers align their businesses with emission reduction goals.

LEVER 3: SYSTEMIC INTERVENTION

Besides guiding member FIs' climate action, CCIs can also use their influence to promote systemic change. They can serve as platforms that amplify and coordinate FIs' systemic interventions **(see → FI Lever 4)**, uniting members behind a common narrative. Additionally, they can assume the role of a central interface with regulators advocating for the integration of voluntary climate commitments into formal regulations.

However, CCIs face the challenge of driving regulatory reform while operating within the very system they seek to change (Voß and Schroth, 2018). In this system, powerful financial actors resist phasing out fossil fuel assets, working to maintain the status quo and obstructing climate action. For example, anti-climate groups in the US accused the Net-Zero Insurance Alliance of violating competition laws, resulting in several insurers withdrawing from the Alliance (Smith and Bryan, 2023). Similarly, GFANZ, appears to have yielded to political pressure scrutinising sustainable investment and ESG (Reclaim Finance, 2022). Concerns have also emerged regarding the lobbying activities of some GFANZ member institutions which have been linked to efforts opposing climate policies, potentially undermining the alliance's objectives (Bindman, 2022; InfluenceMap, 2022b; Ceres, 2023). These challenges highlight CCIs' struggle to oppose political pressures, especially in the US and Europe. Instead of yielding, they must actively lobby for regulatory reform.

Given the limitations in CCIs' accountability mechanisms **(see → CCI Lever 2)**, voluntary climate commitments need to evolve into legally mandated requirements that underpin the entire economy (UN HLEG, 2022; Hidalgo-Oñate, Fuertes-Fuertes and Cabedo, 2024). Initially designed as temporary mobilisation platforms to bridge policy gaps through voluntary governance (Hale, 2022), many CCIs now face the reality that these gaps persist (Taskforce on Net Zero Policy, 2024). Rather than operating indefinitely in a voluntary capacity, CCIs must acknowledge their transitional role and actively push for regulatory reforms. To achieve meaningful climate action at scale, they must go beyond self-regulation and advocate for robust, legally enforced frameworks that dismantle existing legal and economic barriers, ensuring climate commitments translate into lasting structural change.

With the changing political landscape, the role of CCIs in resisting the influence of powerful interests and safeguarding, ideally advancing, climate action is more critical than ever. The following outlines key promising practices for CCIs to drive impactful systemic intervention and they are exemplified in → **Box 7**:

3a. Lobbying for climate progressive regulatory frameworks

CCIs can help facilitate systemic change by lobbying governments for policy reform to incentivise FI climate action. Their advocacy could aim to introduce and strengthen the regulatory and market environments for sustainable finance **(see more → Chp. 4)** while removing systemic barriers embedded in existing regulations. The latter includes integrating climate risks into fiduciary duties and amending anti-trust laws that are currently used against collaborative climate action among FIs (Holmes, 2023). Since lobbying often takes place in political environments resistant to climate action, CCIs must frame the narratives around their lobbying efforts strategically, emphasising, for example, the systemic risks that climate change poses to the financial sector. CCIs must remain proactive in pushing back against regulatory pressures that seek to stall or dismantle essential climate frameworks.

Specific activities CCIs can do include establishing collective position papers, participating in public consultations, and shaping discourse at high-level platforms like COP or G20. More than ever, lobbying efforts need to be directed at the national level, focusing on the governments where initiatives are headquartered or where member institutions are based. To strengthen their arguments, CCIs can draw on members' experiences, highlighting lessons from frontrunners and challenges faced by others.

3b. Requiring member FIs to advocate for regulatory reform

CCIs could require their members to endorse their policy positions and advocate for these directly with the governments of countries where FIs have their headquarters and of countries where FIs are active, ensuring alignment between the initiative's goals and the actions of its members. For instance, members could be required to sign supporting petitions for measures like finance sector disclosure requirements in the EU or integrating ESG considerations into investment duties in the US, or endorse broader initiatives, such as the Fossil Fuel Non-Proliferation Treaty (Fossil Fuel Non-Proliferation Treaty Initiative, 2025).

3c. Establishing pathways for legal adoption of voluntary measures

CCIs can be instrumental in advocating for a transition from voluntary to legally required climate measures, driving economy-wide Paris-aligned decision-making (Hale et al., 2022). CCIs that are set up with a hybrid institutional framework involving both voluntary action **(see → CCI Lever 2)** can work directly with policymakers to ensure that their recommendations and challenges are recognised when setting up a voluntary framework, to ease adoption by the regulatory framework (Lang and Messenger, 2024; Morozov et al., 2024).

Box 7

Systemic interventions in practice

Most CCIs are not effectively utilising their **lobbying power (3a)**. Currently, none of the CCI we assessed is actively lobbying against antitrust and competition being misused to prevent voluntary climate action **(see → Chp. 4)**. While NZAOA has issued position statements on governmental carbon pricing, the oil and gas sector, and thermal coal, it has faced criticism for the adoption of its thermal coal position by members (Reclaim Finance, 2024).

Requiring member FIs to **advocate for regulatory reform (3b)** is not a standard practice across CCIs. NZAOA is one of the few initiatives that incorporates policy advocacy, requiring members to adopt individual policies aligned with the Alliance's position within twelve months, or explain why they do not (UNEP-FI Net Zero Asset Owners Alliance, 2022). Similarly, CA100+ calls for engagement with policymakers to address sectoral barriers in line with the Paris Agreement's 1.5°C goal. However, it leaves the determination of the necessary policy engagement topics up to the investor networks it collaborates with (Climate Action 100+, 2025). PAAO does not specifically call for policy alignment in its commitment but encourages asset owners to ensure that any direct and collective policy advocacy supports the regulation needed to achieve global net-zero emissions by 2050 or sooner (Paris Aligned Asset Owners, 2025b).

Within our sample, there is no public evidence of CCIs trying to **establish pathways for the legal adoption of voluntary measures (3c)**. CCIs outside of our sample, examples such as the Task Force on Climate-related Financial Disclosures demonstrate that hybrid institutional approaches combining efforts from state and non-state actors, supported by state-provided mandates can produce voluntary standards that are integrated into regulation.

/ ∧ 04

THE ROLE OF GOVERNMENT AND REGULATIONS IN LOWERING STRUCTURAL BARRIERS TOWARDS PARIS-ALIGNED FINANCE

While CCIs can help to address some of the barriers that FIs face individually in exercising climate action, the leverage of their collective action is limited by their voluntary nature. The standards and targets they promote, even when ambitious and aimed at credible impact levers of FIs, are not binding. The lack of binding rules and effective incentives reflects a persistent market failure (Stern, 2022), one that regulation, given its authority to mandate, supervise, and enforce, is uniquely positioned to address.

Yet to date, regulation in most jurisdictions has failed to provide the required intervention at scale. So far financial regulators have primarily focused on correcting information asymmetries rather than market failures (Ryan-Collins, 2019). Most regulatory action to date **has centred on climate-related disclosures**, with notable developments in the EU, UK, and US. While improving transparency is important, regulatory interventions that require or incentivise concrete climate action, and price in climate risks in a forward-looking way, remain largely absent.

Another major barrier to more ambitious regulation lies in the **inflexible political economy** in which regulators operate. Any regulatory reform that extends beyond disclosure-based measures represents a significant intervention in traditionally market-oriented financial systems, an approach that can be politically contentious and difficult to advance. While there may be broad recognition of the need for such reforms to address structural market failures, such as the tragedy of the horizon, their implementation is often highly complex and context-dependent, with practical pathways varying substantially across jurisdictions.

This chapter takes a different approach from the previous two. While the FI and CCI chapters identify specific impact levers to strengthen their contribution to climate action, here we do not yet see sufficient evidence or momentum to propose a practical toolbox of regulatory levers. Instead, we focus on identifying where the key gaps lie in the current regulatory frameworks and prevailing market conditions at the institutional and systemic level, and the real-economy interface.

ABSENCE OF PARIS-ALIGNED REGULATORY FRAMEWORKS

At the **institutional level**, FIs are legally bound by fiduciary duties to act prudently and in the best interests of their current and future beneficiaries. Yet, traditional interpretations often focus narrowly on maximising short-term pecuniary returns, neglecting the long-term climate risks (ClientEarth, 2024). This lack of clarity, combined with short-term market pressures and insufficient legal requirements, has led many trustees to be uncertain about whether, and to what extent, they must factor in climate considerations when making investment decisions without facing legal repercussions (ShareAction, 2024). In some jurisdictions like the US, where

anti-ESG sentiment is on the rise, litigation even penalises fiduciaries. Court actions against ESG investment reinforce the perception that climate considerations fall outside the traditional scope of fiduciary obligations (Heineken and Reisch, 2023).

At the **systemic level**, current prudential regulations, which govern FIs' capital adequacy, liquidity, and risk management, do not sufficiently account for climate-related financial risks (D'Orazio, Popoyan and Monnin, 2019; D'Orazio, 2023). Existing capital adequacy and liquidity requirements, as ruled by the Basel III framework, do not differentiate between high-carbon and low-carbon assets, creating an inherent 'carbon bias' (D'Orazio, Popoyan and Monnin, 2019; D'Orazio, 2023). For example, liquidity rules may inadvertently disincentivise banks from financing green projects, which are often perceived as riskier due to their longer payback periods. These rules indirectly benefit carbon-intensive projects from lower risk weights due to their higher liquidity, despite facing greater risks of becoming stranded assets (Campiglio, 2016; Durrani, Rosmin and Volz, 2020).

At the **real-economy level**, FIs operate in a fragmented policy environment where climate-related financial ambitions are undercut by contradictory real-economy regulations. A 'policy gap' exists where voluntary net-zero commitments of financial institutions fall short of driving systemic change because governments have yet to provide the necessary regulations, incentives, and infrastructure for the real economy (Stockholm Environment Institute, 2024). When financial and real economy regulations send conflicting signals, FIs face challenges in implementing a credible transition plan (Aldersgate Group and CUSP, 2023).

Although robust evidence on effective regulatory levers is still lacking, we expect three priority areas where financial authorities can support the functioning of the financial sector's governance chain:

- Reform fiduciary duties to recognise long-term climate risk and integrate double materiality.
- Introduce prudential regulations that reflect climate risks, for example through climate-adjusted capital requirements, sectoral exposure limits, and mandatory stress testing.
- Align financial regulation with real-economy policies to ensure coherent investment signals. Without action across these domains, climate alignment in the financial sector will remain piecemeal and ineffective.

Box 8

First steps towards Paris-aligned regulatory frameworks?

The UK has emerged as a pioneer in integrating climate risk into fiduciary duty. The Financial Markets Law Committee (FMLC) clarified in its 2024 guidance that climate change is a financially material risk, mandating that pension trustees account for climate impacts in their decision-making, warning that failure to do so could constitute a breach of fiduciary duty (Financial Markets Law Committee, 2024). The report categorically rejects the notion that trustees can rely solely on existing legislation, stating that disregarding climate risk due to uncertainty is not legally defensible. Proposed amendments to the Pension Schemes Act aim to codify this requirement (Timms, 2024). This aligns with the UK Stewardship Code 2020, which sets clear expectations for asset managers and owners to integrate ESG factors, including climate change, into investment decisions, requiring signatories to disclose their implementation strategies (FRC, 2020).

At the broader policy level, the EU has positioned itself as a leader in embedding climate considerations across financial and economic regulation. The European Climate Law establishes a legally binding commitment to climate neutrality by 2050, forming the foundation for key policies such as the 'Fit for 55' package, the Effort Sharing Regulation, and the EU Emissions Trading System, all of which drive emissions reductions across multiple sectors (European Council, 2025). These policies are complemented by sustainable finance tools such as the EU Taxonomy and the Sustainable Finance Disclosure Regulation, which aim to direct capital flows toward sustainable activities. By aligning financial oversight with real-economy decarbonisation measures, the EU has set a precedent for regulatory coherence.

ABSENCE OF PARIS-ALIGNED MARKET ENVIRONMENT

At the **institutional level**, the perceived risk profile of sustainable investments represents a key market barrier. FIs typically view Paris-aligned investments as carrying higher technological, regulatory, and market risks compared to conventional investments, leading to risk premiums that increase financing costs (Montague, Raiser and Lee, 2024). This risk perception is particularly acute in emerging markets where institutional, political, and financial risks compound climate investment challenges. Similarly, the risk perception impacts emerging low-carbon technologies, given the high amount of upfront capital investment involved, which makes them more sensitive to the high cost of capital. Although some public-private partnership platforms exist to mitigate these obstacles, de-risking mechanisms such as blended finance remain underfunded, offering only a fraction of the trillion needed annually in emerging markets and developing economies (NGFS, 2023a; Convergence, 2024)

At the **systemic level**, monetary policy and central bank interventions can play a crucial role in shaping market incentives. However, most central banks continue to assume a 'market-neutral' approach, which may be suboptimal in the presence of externalities (Schnabel, 2021). This neutrality approach prevents an efficient allocation of resources, resulting in the lack of incentives to favour green lending, as central bank operations neither reward climate-positive portfolios nor penalise polluting ones. In the absence of robust climate consideration mandates, market signals remain weak and fail to reflect the true societal cost of carbon. The COVID-19 pandemic demonstrated that central banks can act decisively during crises, raising the question of why climate risks, which pose long-term systemic threats, do not receive the same level of urgent response (Dikau, Robins and Volz, 2020).

We suggest two areas where more targeted intervention is needed to derive impact levers to improve the financial market environment for Paris-aligned investment:

- Scale de-risking tools like blended finance and public guarantees to lower the cost of capital, especially in high-risk and emerging contexts.
- Explore green monetary policy tools, such as climate-adjusted collateral rules and asset purchases, to steer market incentives in alignment with long-term climate goals.

Box 9

First steps towards Paris-aligned market environments?

By de-risking climate-related investments, these institutions create the enabling conditions for markets to respond. The European Investment Bank, for example, ceased financing unabated fossil fuels in 2021 and aims to mobilise EUR 1 trillion in climate investments by 2030 (European Investment Bank Group, 2020). Instruments like InvestEU, which is backed by EU budget guarantees, are designed to attract private capital into sustainable infrastructure, innovation, and SMEs (European Union, 2025). The UK has followed a similar path: its Green Investment Bank (GIB), launched in 2012, pioneered the use of first-loss public capital to crowd in private investors in clean energy. Although later privatised, the GIB's legacy lives on in the UK Infrastructure Bank (UKIB), created in 2021 with GBP 12 billion to support both climate action and regional economic development. UKIB offers debt, equity, and guarantees to make climate-related projects investable (GI Hub, 2019). In the US, the 2022 Inflation Reduction Act, marked a major shift by establishing a USD 27 billion Greenhouse Gas Reduction Fund to build a national green bank network and expanding the Department of Energy's loan guarantee authority to support large-scale clean energy ventures (U.S. Department of Energy, 2022).

Complementing these public finance efforts, central banks have also begun shaping the financial system to be more Paris-aligned. The European Central Bank (ECB) has announced plans to incorporate climate considerations into its collateral frameworks and corporate bond purchases, tilting these operations toward issuers with higher climate performance (ECB, 2022). Similarly, the Bank of England (BoE) has oriented its Corporate Bond Purchase Scheme toward firms with credible decarbonisation plans, targeting a 25% reduction in carbon intensity by 2025 and full alignment with net zero by 2050 (BoE, 2023). Rather than pursuing outright divestment, BoE officials highlight the importance of incentivising corporate transition through market-based signals.

CONCLUDING REMARKS

Despite the central role that private FIs must play in driving the transition to a low-carbon economy, the financial sector remains fundamentally misaligned with climate goals. Capital continues to flow disproportionately to fossil fuel activities, while genuine investment in green and transitional solutions remains far below what is needed to meet the Paris Agreement targets.

Achieving meaningful climate action from the financial sector requires an integrated governance chain across three levels: individual FIs, CCIs, and regulators. However, this chain is currently fragmented and incomplete.

At the institutional level, FIs face multiple structural barriers that constrain their ability to drive real-economy decarbonisation. These include limited managerial control over clients' and investees' emissions-intensive activities, information asymmetries, and insufficient access to credible, forward-looking data. FIs also operate under finance-first mandates that prioritise short-term returns, with few incentives to integrate climate considerations into lending or investment decisions. Internal governance challenges, such as a lack of senior leadership commitment, weak integration of climate metrics into remuneration structures, and capacity gaps, further restrict effective implementation.

CCIs have the potential to address some of these barriers by fostering coordination, amplifying ambition, and building capacity across institutions. Yet, despite their visibility and scale, most CCIs have failed to translate commitments into credible, consistent action. Many have prioritised broad participation over rigorous standards and accountability, undermining their effectiveness and exposing them to accusations of greenwashing.

A key factor underlying this underperformance is the voluntary nature of both FIs' climate commitments and their participation in CCIs, as well as the non-binding standards that CCIs typically set. Without binding rules that embed climate considerations into fiduciary duties, prudential regulation, and financial disclosures, voluntary efforts, whether pursued individually or facilitated through CCIs, remain evidently insufficient. The absence of clear legal mandates and enabling market environments weakens the financial sector's ability and willingness to act at the pace and scale required.

Nonetheless, promising practices, particularly at the FI and CCI levels, do exist and continue to emerge. A number of frontrunner institutions and initiatives are pioneering impactful approaches. However, these efforts remain isolated and lack the widespread support and reinforcement that can only come from the regulatory level. A fully intact governance chain, with coordinated action from individual institutions, collaborative initiatives, and regulatory frameworks, is needed to trigger the systemic shift required across the financial sector as a whole.

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ANNEX

NOTE ON SAMPLE SELECTION FOR PROMISING PRACTICE ANALYSIS

FI selection

To identify FIs demonstrating promising practices across a broad spectrum, we focused our screening on banks and asset managers headquartered in the EU, UK, and US. This geographic focus was informed by existing evaluations from established research institutes and think tanks, including (but not limited to) Reclaim Finance, Institute for Climate Economics (I4CE), ShareAction, InfluenceMap, Capital Monitor, World Resources Institute, and the Climate Policy Initiative. These sources are referenced in the corresponding promising practice boxes. We prioritised institutions that consistently appeared in multiple assessments, using frequency of inclusion and high rankings as indicators of credibility and performance. Cross-referencing results across different methodologies helps reduce individual bias and suggests a level of consensus regarding an FI's climate performance.

It is important to acknowledge certain methodological limitations in this study. Selection bias may arise, as ranking methodologies and criteria vary across institutions and are not always directly comparable. In addition, the sample may underrepresent smaller FIs or those based outside of the selected regions due to the geographic and institutional scope of the underlying assessments. Nevertheless, this does not preclude the inclusion of standout 'outlier' institutions from other regions or categories if they demonstrate noteworthy practices.

CCI selection

For initiatives, the sampling approach aimed to capture a broad array of types to reflect diverse impact logics, focal areas, and operational models. Recognising significant variations in objectives, mandates, and theories of change across initiatives, the sample was selected to ensure that our assessment could capture these nuances and identify impactful, innovative practices.

As with financial institutions, this sample is not intended to be exhaustive or fully representative of best-in-class approaches. Rather, it is curated to support efficient screening for impactful practices. Our assessment identified 11 case studies of impactful and innovative practices, which are examined in detailed analyses.

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