

Intelligence MEMOS



From: Glen Hodgson
To: Canadians Interested in Sustainable Finance
Date: November 20, 2019
Re: **CREATING A POLICY FRAMEWORK FOR SUSTAINABLE GREEN FINANCE**

Action on green finance is taking place in many places and in many directions, but there are still many gaps, with no coherent policy framework in place. What would such a framework look like?

The expert panel on sustainable or green finance in Canada released its [report](#) in mid-June, which was [discussed](#) in two earlier Intelligence Memos. It emphasized the private sector is leading the development of the overall Canadian market for green finance, as it should be. A recent C.D. Howe Institute forum on green finance provided solid evidence that many private sector financial institutions are building green finance lines of business – including insurance and other risk management products addressing the impact of climate change, green bonds, structured and commercial financing, and capital formation and equity investment in many fashions.

Private sector financial entities, however, are still struggling with some of the basics – such as appropriate definitions and standards related to green finance, consistent climate-related information, well-defined risk assessment methodologies, and risk management practices. Nevertheless, many financial organizations are stepping forward and undertaking green finance business.

If the private sector is in the lead, what is the role for governments? They can play a useful role in three areas to support the development of green finance.

1. Provide better public information and analysis on the impacts of climate change and assess possible systemic risks to the financial system and economy. Here, the Bank of Canada will be adding climate change impacts to its regular financial system reporting, which is an important step in providing better information to Canadians and to the financial sector. Creating a common database and developing assessment methodologies on the many impacts of climate change would be equally helpful, as a public good.
2. Appropriately regulate green finance activity and risk management by the private sector. Clarifying and standardizing disclosure practices related to climate change risks and business impacts would be an important role for regulators. There is a central role here for OSFI and provincial financial regulators, informed by emerging best practices internationally, and ideally well-aligned across jurisdictions.
3. Define the role of government-owned financial institutions in addressing green finance gaps. Export Development Canada and Business Development Bank of Canada are already active in green finance. They and other Crown financial institutions have many opportunities for an expanded role in the overall green finance market, ideally in a complementary fashion with the private sector. There is also potential for the creation of new targeted “green banks,” as noted by the expert panel.

In addition, more predictable and durable overall climate policy would help to reduce business uncertainty going forward. Better clarity and alignment are needed on the policy tools to be used to reduce greenhouse gas emissions. Putting a price on carbon is the most economically efficient way to reduce emissions. This approach provides a market-based incentive to business and consumers to innovate and adapt. Carbon prices will eventually need to be high enough to have a material impact on consumer behaviour.

Other options – implementing comprehensive regulations, or using subsidies, tax incentives, and government-funded programs – can help reduce emissions, but all come with a higher economic or fiscal cost.

A predictable policy framework would include establishing a roadmap to achieving ongoing reductions in overall GHG emissions, with credible interim targets or mileposts. A roadmap (not a pathway) is the right metaphor to use – since there is more than one possible route to a lower GHG future.

Where to start? The obvious next step is a timely, detailed federal government response to the expert panel, and a plan. And better alignment between the feds and provinces on climate policy is imperative – on a roadmap with credible mileposts, and the smartest, most efficient policy tools for getting there.

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