**ETUC REFLECTION PAPER ON SOCIAL TAXONOMY FOR SUSTAINABLE FINANCE – IDENTIFYING TRADE UNION PRIORTIES AND POLICY PROPOSALS**

**Foreword: setting a TU stake in the sustainable finance agenda of the EU.**

1. Trade unions believe that our mission today is to bounce forward toward a new pattern of development in which we go beyond the GDP for a new social contract that will glue all components of society and economy in a common effort for sustainable and job-rich recovery in a vision of social progress in which all people will be better off.
2. Two dynamics have to be factored in: i. the exit from the pandemic and the change of paradigm linked to green and digital transformations. It requires investments for sustainability, to leave the pandemic behind and “bounce forward”. “**Bouncing forward” is an opportunity to go Beyond the GDP ideology for a new-social-contract**. The UN2030 Agenda moves us in a beyond-GDP era in which all people are better off. This is reflected in an increasing attitude of investors to factor ESG elements in their portfolios. All this calls for a thorough commitment of all concerned people and players to move in the same direction.
3. **The level of engagement is so vast and cutting across all areas of the society and the economy that it brought some to call for a “new social contract**”. In this regard, the UN2030 is the most advance attempt run by the worldwide community to convergence on a new social contract that applies globally. And the business community seems starting recognising that.
4. **For job-rich sustainable recovery and social progress**, private and public investments have to contribute to materialise that vision. The ETUC has proven that sustainable growth, employment and decent work (a SDG8-centred approach) will push the entire agenda forward, building on multi-dimensional feature of goal 8 and the direct positive correlations it has with other SDGs.
5. The concept of social has been stretched in the course of the decades and today it encompasses not only labour but also health, consumption, legality, rule-of-law, education and other societal pillars. **But people and work have to stay at the centre of the agenda**. Gaining support of people is crucial. Creation of quality jobs in a context of sustainable growth is surely pivotal.

**TU INPUTS FOR A SOCIAL TAXONOMY OF SUSTAINABLE FINANCE**

1. **The EU yearns to become the global centre for sustainable finance**. To make it happen the EU is called upon to reinforce its internal market structures (material, immaterial, human capital, companies, legislation, etc.). The EU taxonomy for sustainable investments is an internal market issue but, as far as it will succeed being global leader for sustainable finance, the EU will be able to attract, export, and likely impose, standards worldwide.
2. **Sustainable finance, under certain conditions, can inject sustainability and resilience in our economies**. Sustainable investments could ignite investments for recovery complementing the public ones activated by the EU. For that to happen sustainable investment should become a mainstream industry so giving the EU a competitive advantage to attract and employ patient capitals that give value to environmental and social impact of investments. For that to happen sustainable finance should be genuinely sustainable while current market arrangements do not shelter against forms of rainbow-washing or other speculative activities.
3. **A thriving and genuine sustainable finance industry may deliver positive return to workers with new quality jobs and more economic democracy**. Investments can potentially create additional new jobs, while related sustainability criteria will render more likely that investments will produce quality jobs. However, it will impose some changes in the way the economy performs, investments are allocated, and new elements of economic democracy should be encompassed in its governance structures as well.
4. **The EU Taxonomy should bring benefit to all economic sectors**. In this regard, as it happened for the green taxonomy, the social taxonomy should be solidly framed in article 3 of the TFEU which establishes an internal market that works for the sustainable development of Europe, based, among other things, on balanced economic growth and a high level of protection and the improvement of social and environmental objectives. Making available financial products which pursue socially sustainable objectives could be an effective way of shifting capital flows toward more sustainable activities and this has to be underpinned by a shared, holistic understanding of the social and environmental sustainability of activities and investments.
5. **The EU taxonomy to be credible should be selective and embracing an SDG approach to sustainability**. The ESG approach has not solved the trade-off between social and environmental objectives so far. However, the UN2030 Agenda offers a holistic approach to sustainability and tells us that sustainable finance should select investments that comply with the multidimensional features of sustainability and exclude those that are not able to compel with all dimensions of sustainability. The EU Taxonomy, both green and social, should compel the UN2030 Agenda in full, coherent, comprehensive, integrated manner, in close cooperation with partners and other stakeholders.
6. **Social taxonomy should reward investment that respond to two urgent priorities**. As a first step, clear guidance should encourage activities that qualify as contributing to social objectives that would
7. **address the adverse consequences of the pandemic crisis** on health and employment, starting from a greater commitment to analyse social risks (unemployment, social exclusions, education shortages of the generation currently at school) and social ruptures such as those based on gender, age, migration status, labour market positioning;
8. **help inform investors and clients/consumers** about the investments that fund social sustainable economic activities, or support sustainable corporate purposes, in particular promoting financial education and tackling financial illiteracy.
9. With the taxonomy for sustainable investments, the regulation of the financial market is no longer alien to the setting of social standards in Europe. It becomes part of it instead. **The elaboration of an EU taxonomy for sustainable investments should concur to the achievement of the objectives of the social policy of the EU**. Investors and investee should engage at different level in a way that social labels for investments respond to exclusion/exit criteria, minimum requirements and engagements for progress toward common objectives, regardless of the financial instrument used (equity, bonds, loans, etc.).
10. The ETUC considers that a social taxonomy should include at least:
* **An entry level**, aimed at **ensuring full compliance with the international standards and the European Charter of Social Rights** that compels the majority of such rights and standards;
* **A compliance mechanism**, that concerns respect of EU law and applicable collective agreements;
* **A social progress mechanism**, that commits social investors with the implementation of the European Pillar of Social Rights.
1. **And all institutional, economic and social actors commit to achieve social progress moving into shared policy frameworks that set aims, monitoring and impact criteria**. The European institutions and member states jointly committed to pursuing the principles enshrined in the European Pillar of Social Rights in support of sustainable and inclusive growth; the Action Plan implementing the European Pillar of Social rights, endorsed by social partners, EU institutions and governments, in Porto on the 7th and 8th of May, includes a new social scoreboard and a set of social targets that makes social progress consensually measurable according to a commonly agreed metric and methodology; it should also be recalled that all economic and social agents are called upon and committed to provide their own contribution to achieve the objectives set in the principle so for of the EPSR according to the priorities identified in the Action Plan.
2. The ETUC considers that the social taxonomy should build on these 3 criteria:
3. A) **An entry level based on compliance with international (labour) standards and human rights:** If Europe wants to be global leader, the Social Taxonomy should:
* Transform the minimum safeguard clause in the social as set in the Green Taxonomy into a sin qua non requirement for the social taxonomy, especially for activities or corporate purpose that extend their operational geographical scope beyond the EU border;
* Refer at least to OECD Guidelines for Multinational Companies, UN Guiding Principles on Business and Human Rights, including the declaration on Fundamental Principles and Rights at Work of the ILO, and the International Bill of Human Rights applicable to specific activities implemented or purposes pursued by the financial instrument adopted.
1. As a result the Social Taxonomy should provide a framework that requires (sine qua non) investors and investee have to demonstrate full respect and corporate due diligence in ensuring abidance by internationally recognised standards and being active in promoting them.
2. B) **A compliance mechanism, promoting legality and rule-of-law:** As an act of internal market, the Social Taxonomy should:
* require respect and also engagement with the implementation of the EU acquis and compliance with the EU Charter of Fundamental Rights and fundamental rights enshrined in the EU Treaties;
* contribute to the respect of rule-of-law and legality in the EU.
* Require respect of applicable collective agreements when implementing activities financed with sustainable finance instruments or setting key performance indicators when the “S” factor comes from a securities promoting a corporate purpose;
* Identify regulations, directives and recommendations that are part of the EU acquis and provide minimum standards or harmonisation of labour market, workers’ protection, non-discrimination, access to work + skills + education, and social protection and occupational welfare.
1. Thus, the Social Taxonomy should provide a framework that requires progress under one of the provisions set in the EU law and not be in detriment of the rule-of-law, and require respect of collective agreements and no-harm to collective bargaining.
2. **C) ENGAGING WITH SOCIAL PROGRESS**. The EPSR is a valuable framework for investors and investee that want to walk the way of sustainability because it:
* gathers the widest **consensus** (see Porto’s event) where substantial contribution can be easily identified, with a good level of granularity, covering a good number of types of substantial contributions;
* offers a **methodological framework** for investors and investee. It is supported by soft and hard law that determine activities of substantial contribution that implement rights, contribute to specific policies and sub-policies, progress toward common objectives, identify enablers of such policies;
* Covers the most **relevant areas** where social investors are currently seeking for impact: education, inequalities, opportunities , welfare, job creation, etc. but comprehensive enough to adapt to the core business of the operations in which the “social activity” is implemented;
* It is backed by (5-years old) scoreboards, targets and metrics that set **level of ambition and measure of impact**, and reporting can be combined with progresses of public investments under the RRF so to find consistency between public-sector and private sector frameworks.
1. The Social Taxonomy can provide a framework that requires progress under one of the principles of the EPSR and should not result be in detriment of the objectives set in other objectives.
2. **This approach to EU Taxonomy could also serve as the basis for other economic and regulatory measures, such as social investments in the InvestEU**. This 3-dimensional approach should enable the development of future Union policies in support of sustainable financial products and the eventual establishment of labels that formally recognise compliance with those standards for socially sustainable financial products and the eventual establishment of labels that formally recognise compliance with those standards across the Union.
3. **Safeguard clauses have to be considered to avoid that social taxonomy may interfere with policy areas that fall in the remit of social partners**. In case of interferences or risks of interference, autonomy of social partners prevails because social partnership is expression of a more extensive solidarity. Respect of collective agreements and promotion of collective bargaining should be an inherent and indivisible component of the EU social taxonomy. This element is crucial to define practice-based and process-based social “activities” or social “purposes”.
4. **A more open and transparent governance of the market of sustainable finance is needed**. On governance side the social taxonomy has some corollaries that touch upon specific interests of workers and this should lead to a quality leap in the process of democratisation of the European economy.
5. Specific risks linked to governance of sustainable investments that relevant to workers:
* entrenchment of powers, capture of decision-makers and controllers by specific interests and unweighted representativeness of stakeholders;
* ineffective allocation of resources that create distortion or penalise workers in excluded sectors;
* misalignment of use of proceeds, corporate behaviours and KPIs, their monitoring and reporting mechanisms, with the overall sustainability requirements.

26. The ETUC suggests the following provides for:

* Market designing: structured and permanent consultation of social partners in the shaping and regulating the sustainable finance market;
* Sectoral aspects: mutual engagement of finance industry community with trade unions to embrace the just transition concept and forge it in a way that all businesses in all sectors (public and private) will have the same chances to benefit from sustainable finance;
* Company level: Employees’ participation to be considered a criteria that reinforces investors’ active engagement and conducive to better governance of sustainability processes.
1. **If the workers’ position will be neglected, it would generate a negative bias on the development of the market of socially sustainable financial products**. The EU taxonomy builds on converging interests of consumers (of the finance industry?) and investors that want to participate in the sustainable finance market having access to reliable information, without suffering from information gaps and having awareness of the impact of their choices and decisions. This approach risks to exclude the position of workers. In general, democratisation of the economy stems from a larger and inclusive access of people to the financial market which implies investments in education (increasing financial literacy). Financial literacy starts from the workplace.
2. **Some European experiences show that such democratisation of the economy can start from the workplace and employees’ participation schemes**. If the EU cultivates the ambition to be a global centre for sustainable finance, its regulatory and implementing model should imply a reinforced framework for employee participation that has redistributive and governance implications, whose scope covers all European businesses and state-owned economic that receive sustainable investments, and includes investments in know-how and financial literacy in favour of people, starting from workers.
3. The Directive on Sustainability Reporting, replacing the Directive on Nonfinancial Reporting, would establish a procedure for defining a single set of European reporting standards and require large European companies and companies (listed on an EU-regulated exchange) to publish sustainability information as part of their annual management report. The current proposal is not adequately supportive to a better involvement of employees and not aligned to the ambition of a EU taxonomy for sustainable finance of designing, elaborating, and monitoring impact of non-financial information.
4. **The EU strategy for sustainable investments should not be seen as a substitute to the role of the state** (and its administrative articulations) to deliver the common good made of protections, welfare structures, infrastructures and quality services that are needed to make a fundamental rights and quality of life not formal but real. The investments incentivised by the social taxonomy should be complementary to social investments of the RRF.
5. **Finally the EU social taxonomy should business models that value social return. In that regard social enterprise economy** should be rewarded as far as they privilege social return instead of extracting excessive resources for their shareholders and creditors and specific instruments for SMEs should be introduced without exempting them from sustainability requirements.

ANNEX: **SUSTAINABLE FINANCE: Defining the market**

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The sustainable finance market represents today less than 2% of the global financial market if we consider the fixed-income debt instruments (such as bonds) only. Some estimate that it may reach 5% of the overall financial industry in Europe. Some sources say that, in absolute terms bonds traded under the sustainable finance industry amount to 1,000 billion dollars worldwide, with an annual issuing of 250 billion dollars per year for green bonds. According to some, social bonds have suddenly increased in 2020 overcoming the 100 billion dollar of issued bonds, thereby confirming a great interest that financial industry attaches to social impact of their investments but it is premature to estimates whether this will remain a permanent trend (see graph below).

Sustainable investments are usually referred to as ESG investments. Investments aimed at tackling climate change and the environmental impact of production are the largest share and were pushed up by the Paris agreements and the sense of urgency that a wider part of the population attach to the environmental emergency. Social investments record a fast increase since the SDGs clearly displayed the social boundaries of development. Good governance comes from the corporate social responsibility practices and G bonds (or securities) represent a relevant share of sustainable investments to which investors more intuitively attach an added value.

ESG stays for:

E = Environment

S = Social

G = Governance

Investment funds prefer equity but fixed income instruments are considered a promising market for sustainable investments. Bonds issued in the framework of sustainable finance can be green or social based on the promise that the proceeds will be used to enact green or social projects. When they mix green and social actions they are called sustainability bonds. Recently a new category appeared that closely follows the SDG precepts. They are called sustainability-linked bonds.

Social, Green and Sustainability Bonds are traditionally defined use-of-proceed instruments. It means that the resources made available by issuing sustainable bonds will be used to address a green challenge or a social one or both as declared in the information to the market that backs the issuing of the bonds. The proceeds should be used to increase assets that the issuer allocates for the achievement of the declared sustainability objective. This has its consequences in terms of disclosure, reporting and monitoring. These kind of bonds deliver a promise concerning the impact of a specific action but not on the overall impact of the economic activity of the issuer (state, corporation, local authority, group of enterprises, etc.). These kinds of bonds represent almost the totality of the sustainability bond market.

The sustainability-linked bonds, instead, support a corporate purpose to stick with the multi-dimensional feature and indivisibility of the UN2030 Agenda. So, they are not linked to a specific action (use-of-proceeds) but they promise that the overall action of the corporation is devoted to the achievement of sustainability patterns (corporate purpose). Its credibility is conferred to Key Performance Indicators (KPI) that in this case assume a relevant role. It means that proceeds may be committed not necessarily in assets but can for instance finance operational costs of the issuer. It has pros and cons. This is a new generation of financial instruments that therefore occupies a tiny segment of the market but are estimated to spread out rapidly. They value about 10 million dollars in 2020.

Half of the bonds classified in the sustainable finance market are issued by government or state-owned entities, one third can be attributed to private corporation while this instrument is almost inaccessible to SMEs and local authorities. The reason could be linked to entry and steering costs that incur to fulfil the requirements which sustainable financial instruments are subject to.



Finally, it has to be considered that (*strictu sensu*) social economy enterprises are not factored in the sustainable finance market even if such kind of businesses have given proof to pursue sustainability goals as part of their own mission and are made of assets, equities and debt instrument as all other businesses.

Many expect that the financial markets will expand driven by liquidity supply. In particular, bonds (debt) are expected to grow faster than equity. Sustainable finance will have its chance to thrive in the European market. Indeed, the Euro area financial market is esteemed to grow faster than the rest of the world. This is a relevant opportunity if the EU will be able to build an internal financial market that better serves the real economy and less prone to speculative practices.

The S factor is also gaining relevance in sustainable finance. It seems that the pandemic crisis has pushed the S factor on the forefront and investments are now reflecting this new awareness concerning risks coming from social disruptions. However, according to some calculations, the global social investment portfolio dos not go beyond 100 million even if the issuing of EU bonds can provide a relevant boost to this figure.