



22 June 2022

FIA EPTA response to the UK Government [Call for Evidence](#) to support its update of the Green Finance Strategy

The European Principal Traders Association (FIA EPTA) welcomes the opportunity to respond to the United Kingdom (UK) Government Call for Evidence to support its update of the Green Finance Strategy.

FIA EPTA represents 24 independent European Principal Trading Firms (PTFs) which deal on own account, using their own money at their own risk, to provide liquidity and immediate risk transfer in exchange-traded and centrally-cleared markets for a wide range of financial instruments, including shares, options, futures, bonds and ETFs. FIA EPTA's members are based in the UK (~70% of our members have been licensed by the FCA) the Czech Republic, Germany, Ireland and The Netherlands.

Our members are independent market makers and providers of liquidity and risk transfer on trading venues and to end-investors across Europe. Market making and liquidity provision (also referred to as principal trading or dealing on own account) is a distinct activity that is undertaken by non-systemic investment firms rather than banks, in a highly dispersed and varied ecosystem of independent Principal Trading Firms. These firms operate in an innovative and competitive fashion leading to a vibrant, dynamic and diverse ecosystem which massively reduces interconnectedness and increases substitutability. This fundamentally reduces systemic risk whilst improving market quality and lowering costs for retail and institutional investors alike.

FIA EPTA members welcome the actions and responsibilities taken by the UK Government during COP26 in Glasgow and the work toward the common goals of reaching climate neutrality in 2050.

FIA EPTA is committed to supporting policymakers and regulators in ensuring the success of the sustainable finance project at all levels of the capital market ecosystem. We would welcome the opportunity to provide further background to the UK Government on the issues raised in our response.

Capturing the opportunity

Headline Questions

1. What are the key characteristics of a leading global centre for green finance?

FIA EPTA members believe that the UK Government is at the forefront of the global fight against climate change and mitigating its impact on citizens. The UK Government showed its leadership during COP26 in Glasgow and with the review of many legislative initiatives as also this Call for Evidence shows.

It is critical that the UK Government does not lose momentum if the UK is to remain a global centre for green finance. FIA EPTA members express the hope, therefore, that the UK Government will continue to be an ambitious standard-setter, drawing on the high level of experience and professional excellence which is present within the broader UK capital markets ecosystem. Doing so will place the UK in a position to effectively influence global regulatory approaches and build bridges with other jurisdictions. While global jurisdictions may have different opinions on how to approach the fight against climate change, we see several clear allies across the globe, including the EU, that the UK could effectively work with to ensure that finance can efficiently contribute to the green transition while minimising undue regulatory inefficiencies or uncertainties.

In addition, FIA EPTA members believe that if the UK and EU work together on standards and regulatory initiatives, it will benefit the UK becoming a hub for sustainable related products and companies that work on climate solutions.

2. Do you consider the UK's green finance regulatory framework to be world-class?

FIA EPTA members view the UK's green finance regulatory framework as one of the best in the world as it addresses many issues around environmental and social issues while keeping in close contact with industry and interest groups. This is key to a smooth green transition where all sectors should work together toward common goals. As also highlighted in question 1, FIA EPTA members believe that for the UK to continue to be a global standard setter it has to work together with other jurisdictions to focus on driving competitiveness and flexibility while keeping high and ambitious goals.

3. To what extent does the UK's private and public sectors have appropriate skills/capacity to attract international green finance flows?

Speaking for FIA EPTA's own membership, we can confirm that our member firms, including the large majority of members that are licensed in the UK, are significantly increasing their liquidity provision activity in green finance products. A recent FIA EPTA survey found two-thirds of our member firms are expanding their activities in the ESG space¹. While market making firms surveyed are most active in supplying liquidity in ESG futures (50%), they are starting to see a

¹ <https://www.fia.org/marketvoice/articles/two-thirds-european-market-makers-plan-expand-esg-liquidity-provision>

growing demand from both institutional and retail investors in ESG exchange-traded funds (45%).

In this way, market making firms can play a key role in facilitating the green transition by providing constant liquidity and making ESG products more attractive and available to other market participants. This helps minimise the cost of investing in ESG products, which can help investors reorient capital to sustainable investments. We would call on the UK Government, therefore, to seek to optimise conditions for the availability and adoption of exchange-traded green finance products, which can be a useful additional tool for both professional and retail end-investors to direct their capital to the green transition while managing their financial investment risks.



4. What are the UK’s comparative strengths and weaknesses in its green finance offering compared to other international financial centres? What are these for:

b) Capital markets

FIA EPTA Members believe that the UK Government and regulators have created a financial centre that is open and welcoming to new and current businesses. UK regulators are viewed as very knowledgeable and as having a lot of experience. With COP26, the UK Government showed their commitment to the green transition and its commitment to greening the financial system.

As stated in the responses to previous questions, FIA EPTA members believe that the UK Government should effectively influence global regulatory approaches and build bridges with other jurisdictions, including the EU. Ensuring that finance can efficiently contribute to the green transition while minimising undue regulatory inefficiencies or uncertainties as it could be a weakness for the attractiveness of the UK as a financial centre. As the demand for sustainable products will grow, these products will need to be embedded in mainstream

markets, and so unjustified divergence between jurisdictions could lead to firms choosing to trade in fewer markets, limiting market participation and hindering the delivery of the green transition.

In terms of strengths, the green transition also gives opportunities for the UK to further develop and deepen its capital markets. As the demand for sustainable products grows, these need to be developed and traded on liquid markets. FIA EPTA members believe that the UK could better utilise its deep capital markets, especially the secondary markets to facilitate this growth. The secondary markets enable asset holders to effectively manage their fiduciary duty regarding their sustainable holdings (e.g. to buy or sell ESG products on behalf of end-investors, insurance holders, or pension participants) and to enable sound financial risk management for these end-investors.

To support a mature and healthy secondary markets ecosystem of exchange-traded derivatives and ETFs based on underlying assets needs to be developed alongside the primary and secondary markets for sustainable shares and bonds. This will foster a liquid market for sustainable investment and provide for greater risk management which is needed to ensure that Sustainable Finance is fully embedded into the mainstream of the financial markets ecosystem. As independent market makers and liquidity providers, FIA EPTA members have the expertise and the commitment to supporting this development. Last year, FIA EPTA published its Principles on Sustainable Finance and ESG to explain how we believe our members can contribute to the sustainability goals².

5. How can the UK government measure progress towards becoming a leading global centre for green finance?

FIA EPTA decided not to answer this question.

6. What areas for potential growth – for example emerging financial products and instruments – are there in green finance for the UK financial services sector?

FIA EPTA members believe that the secondary markets are an important part of green finance and the UK financial services sector and are not yet fully utilised. FIA EPTA members believe that sustainable/ESG products should be traded on existing trading platforms so that they can be incorporated into the existing framework and will be better accessible and liquid.

As the demand for sustainable products is growing, and more investors choose to invest in sustainable products the market as a whole should adjust. As market makers and liquidity providers, FIA EPTA members have the ability to support investors with the migration towards a green portfolio. Supplying liquidity in sustainable products and making sure there remains a counterparty to sell 'brown' products to facilitate a smooth transition.

² FIA EPTA Principles on Sustainable Finance and ESG, June 2021: <https://www.fia.org/epta/resources/fia-epta-publish-principles-sustainable-finance-and-esg>.

The listed and cleared derivatives sector can play an important role in the shift towards a green economy. Derivatives products enable asset holders to manage their financial risks, which is crucial for discharging their fiduciary duty and for appropriately managing their long-term investments; thus, the listed and cleared derivatives sector is an important secondary contributor to long-termism.

FIA EPTA members are an important source of liquidity in listed and cleared derivatives, including ESG futures and options. By providing a tight bid-ask spread, climate change-related financial risks can be hedged with minimal cost (contributing to the enabling and mainstreaming of the management of financial risks coming from climate change).

To give an example, FIA EPTA members would like to note an issue with Exchange Traded Derivatives (ETDs) in the EU. FIA EPTA members believe that the sustainable/ESG ETDs market would have much potential for the UK to grow. For now, the current Taxonomy and Sustainable Finance Disclosure Regulation (SFDR) proposals³ in the EU would in effect restrain the use of listed derivatives by market participants and restrict the amount of capital that can be made available for a sustainable transition. Listed derivatives are a key component of mature secondary markets. The recent growth in demand for listed ESG derivatives demonstrates that these products are a core component of sustainable investment strategies, especially since the availability of liquid and transparent derivatives significantly reduces funding and financing costs for equity and bond issuers in primary markets.

In the current EU SFDR draft ETDs would not be recognised as contributing to Taxonomy-aligned investment activities, and yet would still need to be included in the denominator as part of the total assets of the product or portfolio. This proposed approach would unduly disincentivise the use of derivatives in the affected financial products since any exposures to derivatives could only ever contribute negatively to the Taxonomy alignment ratio. This would make it more difficult for end-users to use exchange-traded derivatives for managing their financial risks and in the process undermine the goal of having safe, liquid, and efficient markets that can support the green transition.

FIA EPTA members believe that this area provides a good example of where targeted divergence from current EU proposals could provide the UK with stronger green outcomes and a more competitive Sustainable Finance sector, and we see this as a good opportunity for the UK to develop the growth of the sustainable derivatives markets.

Financing the UK's energy security, climate and environmental objectives

³ Draft Regulatory Technical Standards with regard to the content and presentation of disclosures pursuant to Article 8(4), 9(6), and 1(5) of Regulation (EU) 2019/2088 (JC/2021/50).

Headline Questions

7. **How can the UK support a financial system that leverages private investment to meet the UK's climate and environmental objectives?**

FIA EPTA decided not to answer this question.

8. **How can the UK support a financial system that leverages private investment to meet the objectives of the British Energy Security Strategy, including in areas such as nuclear, hydrogen, carbon capture and storage and domestic oil and gas production, to reduce our reliance on imported fossil fuels as part of a smooth energy transition?**

FIA EPTA decided not to answer this question.

9. **What barriers are there to unlocking private investment to support the UK's energy security, climate and environmental objectives?**

FIA EPTA decided not to answer this question.

10. **How can the UK government assess and measure progress toward financing the UK's energy security, climate and environmental objectives?**

FIA EPTA decided not to answer this question.

11. **How can the UK best facilitate greater private investment into climate change adaptation and resilience activities?**

FIA EPTA decided not to answer this question.

Financing transition activities

Questions

12. **Are there barriers to the mobilisation of private investment into transition activities? If so, what are they and how might they be overcome?**

FIA EPTA members believe that the sustainability/ESG data should be improved because the lack of transparency currently hinders private investment in transition activities.

Almost all (retail) investors rely on data from rating agencies for their investment decisions. For now, there is not enough harmonisation and standardisation between data for investors to make meaningful decisions. For an effective mobilisation of private capital for sustainable products, trust and clarity in the data and products are needed. This uncertainty in the data and products will slow down the shift towards a green financial infrastructure.

Rating agencies should work together with trading platforms and index providers to create a system in which it is easy to understand which ESG parameters the data is based on, reflecting the fact that ESG is a developing area where more and more characteristics are part. FIA EPTA members believe that it should be clear on which ESG characteristics an ESG rating is based, for example in the case of an index, is it based on 'best in class', which means that certain companies could be part of the index that have or contribute to high carbon emissions.

This is mainly because of measurement divergence, meaning that agencies measure the same attribute using different indicators. Next to measurement divergence, weight, scope and aggregation of indicators play a role in the lack of correlation between the different ESG ratings. This makes it difficult, if not impossible, to come up with truly meaningful and harmonised ESG ratings between the different rating agencies. FIA EPTA members believe that regulation is needed so that the same ESG ratings have the same regulation as other data. If the UK does this well it could further cement it's a green financial centre with transparent and compatible data which is needed to reach the climate goals.

13. How can the UK become a leading hub in structuring and innovating on transition finance?

FIA EPTA decided not to answer this question.

14. Is there a role for the UK government to support the development of transition finance markets in the UK and internationally?

FIA EPTA members believe that the UK Government, with the organisation of COP26 and its intent to be a global standard setter, has a pivotal role to play to support the development of the transition finance markets. We believe that the UK should try to work together, in particular with the US and EU, to come to a high standard that reflects the ambitions of both jurisdictions. In addition, the UK (together with the US and EU) should try to work together with other jurisdictions through international bodies and forums to help the development of a global minimum standard.

FIA EPTA members believe the UK Government should continue to work together with market participants on regulatory initiatives, making sure that regulation is calibrated well and is fit for purpose. Making sure that market participants have a better understanding of what is expected will support the delivery of the Government's policy objectives and help the private sector better contribute to the green transition.

Developing natural capital markets

Questions

15. How can the UK best support the mobilisation of private investment to natural capital assets?

FIA EPTA decided not to answer this question.

16. How can the UK government best assess the progress and development of a natural capital investment market?

FIA EPTA members believe the UK Government should target a long transition period to help businesses prepare for the green transition. Conversely, our members believe that too short a transition period risks slowing the green transition and damaging capital markets, with a knock-on impact on the UK's wider financial infrastructure.

Transitioning out brown assets needs to be done over time, as there are not yet enough alternatives to support a rapid transition. FIA EPTA members believe that traditional

companies can play a vital role in the transition, and at this point in time, we are not in favour of delisting/de-investing in companies that are currently deemed 'brown' as these companies have large funds to invest in greening their products. However, the UK Government should set out clear goals and timelines and make companies accountable to work toward climate neutrality and support companies that work on climate solutions.

Ensuring broad access to green finance for local authorities, SMEs and retail customers

Questions

17. How can the UK financial sector support the delivery of the UK's climate and environmental objectives at the local level, whilst also benefitting local growth and communities?

FIA EPTA decided not to answer this question.

18. How can local authorities support the mobilisation of private and public investment to key sectors and technologies for the UK's climate and environmental objectives, whilst also meeting local priorities? What barriers to this are there?

FIA EPTA decided not to answer this question.

19. What is the current state of capability within local authorities to attract investment, and how can it best be supported?

FIA EPTA decided not to answer this question.

20. How can the UK financial sector support SMEs and retail customers to align with the UK's climate and environmental objectives?

FIA EPTA decided not to answer this question.

21. Is there a role for the UK government to facilitate broad access to green finance for local authorities, SMEs or retail customers? If so, what should these roles be?

FIA EPTA decided not to answer this question.

High integrity voluntary markets for carbon and other ecosystem services

Questions

22. How can the UK best support the development of high integrity voluntary markets for carbon and other ecosystem service markets?

FIA EPTA members believe that the voluntary markets for carbon and other ecosystem service markets are important components of the green transition. For market participants to fully engage with these products, the market must be stable and neutral and it must be building

towards a longer-term solution. Again transparency will be key, and FIA EPTA members believe that support for these kinds of initiatives will grow if they are founded on policies that have a clear commitment and timeline.

23. How can we ensure that these markets encourage robust action on the UK’s climate and environmental goals, and appropriately scale up finance flows to support these?

FIA EPTA members believe that to encourage robust action from market participants the UK Government should, for now, maintain support for transitioning the brown markets until the sufficient development of alternative resources. FIA EPTA members believe that in the migration toward sustainable markets, the brown markets have a role to play as they hold lots of funds that can be invested in new, and climate solution technologies. FIA EPTA members believe that it’s better to make sure that brown markets are incentivised to grow towards green and are not being penalised for being or trading brown markets/products.

24. How should the UK harness the economic opportunities associated with high integrity growth in voluntary carbon markets and ecosystem services markets?

FIA EPTA members believe that the voluntary carbon markets need to be transparent, and easily accessible to ensure that trading strategies aren’t too restricted. That way, the spread between the buy and sell-side can be tightened, lowering the cost of trading and making trading quicker and more efficient. Our members think that - with the right regulation - the UK is well-positioned to become a global centre for the carbon markets.

FIA EPTA members believe that new kinds of products, such as the carbon markets, should be treated equally to established products as artificial barriers will create less trust in the market and it will be more difficult to determine the price for products, leading to potential bubbles in the market.

Finally, FIA EPTA would encourage the UK Government not to overregulate the carbon markets. Making sure there is an open and transparent trading infrastructure in which different trading strategies can be executed is vital for the uptake of products. Ensuring there is no limiting of market making and liquidity provision will be important as these help with price discovery and market stability and in addition, are an important factor of risk management.

25. How can UK environmental and economic regulators increase demand for high quality, accredited ecosystems services?

FIA EPTA decided not to answer this question.

Greening the financial system

Headline Questions

26. What are the key characteristics of a Net Zero-aligned Financial Centre? How would these characteristics apply to a typical UK-based:

FIA EPTA decided not to answer this question.

27. What market barriers are there to the integration of environmental-related factors into financial decision-making?

FIA EPTA decided not to answer this question.

28. What should the role of the UK government or regulators be to support the greening of the financial system? How could they go further?

29. How can the UK government measure progress towards greening the financial system?

FIA EPTA decided not to answer this question.

Providing the market with the right data

Questions

30. What steps can the UK government take to support a robust investment data ecosystem to attract green finance flows?

FIA EPTA members believe that data is an important component of the bases on which investors make investment decisions. This includes transparency around the methodology and objectives that were used. For now, FIA EPTA members acknowledge that there always will be differences between data from data providers/rating agencies. However, due to the absence of standardisation and harmonisation of the ESG data, the average correlation between the data is wider. FIA EPTA members believe that through regulation, more transparency and harmonisation can be reached, aiding meaningful investment decisions and accelerating the UK's green transition.

This is mainly due to the problem of 'measurement divergence', whereby different data providers/rating agencies measure the same attribute using different indicators. Next to measurement divergence, there is also divergence between weight, scope and aggregation of indicators, which plays a role in the lack of correlation between the different ESG ratings. This makes it difficult, if not impossible, to come up with truly meaningful and harmonised ESG ratings between the different rating agencies. FIA EPTA members would like to encourage establishing more standardisation so that the comparability of these ratings increases.

Another important component is the trust in the data. For sustainable/ESG products to reach the same maturity as existing (non-ESG) products there needs to be trust in the underlying data. Any 'green bubble' created due to an absence of accurate data would risk harming the green transition enormously. That is why FIA EPTA members believe that regulation is needed to improve transparency, standardisation and harmonisation to prove why some products are deemed ESG and some are excluded.

31. Are Scope 3 (supply chain) emissions data important for investors to assess and manage climate-related risks and opportunities?

FIA EPTA decided not to answer this question.

32. Is there a role for the UK government to support businesses (of different types and sizes) to make good quality Scope 3 emissions disclosures (including SMEs in the value chain of disclosing entities)? If so, what should this be?

FIA EPTA decided not to answer this question.

Leading internationally

Headline Questions

33. Up to 2030, how can the UK government best support the global transition to a net-zero, nature-positive financial system that is both inclusive and resilient?

FIA EPTA members believe that the UK Government should continue with its global leadership role in the green transition to a net-zero system. The UK Government has already shown its commitment via hosting the COP26 and launching a wide range of regulatory initiatives on incorporating environmental and social components into the financial system. In addition, FIA EPTA members believe that the UK Government should continue to work together with market participants on regulatory initiatives, making sure they are fit for purpose.

For the UK to continue with this leadership role, FIA EPTA members believe that co-operating between jurisdictions is extremely important. Ensuring that finance can efficiently contribute to the green transition while minimising undue regulatory inefficiencies or uncertainties, as barriers could impact the common goals of reaching net zero. The UK has proven expertise and global leadership here, and harnessing this to lead global standard-setting will support the global transition to net-zero and aid the development of an effective market.

In addition, FIA EPTA members believe that the UK Government should continue to invest in climate solutions and create an atmosphere in which market participants are incentivised to contribute more toward the transition. In which brown companies/products still have a role to play and are encouraged to create transition plans and contribute towards the transition and not be punished and/or abandoned too quickly.

34. How can the UK government increase the mobilisation of public and private investment to achieve 2030 climate and nature targets in emerging and developing economies?

FIA EPTA decided not to answer this question.

35. How should the UK government assess and measure progress towards the transition of the global financial system and mobilisation of finance for global climate and nature goals?

FIA EPTA decided not to answer this question.

Building on the Glasgow Leaders' Declaration on Forests and Land Use

Questions

36. How can governments work with the financial sector to help align the global financial system with the Glasgow Leaders' Declaration goal of reversing forest loss and degradation by 2030?
FIA EPTA decided not to answer this question.

37. What support is needed to help firms to factor AFOLU related emissions and potential risks into their strategic planning?
FIA EPTA decided not to answer this question.

Supporting an inclusive transition in emerging and developing economies

Questions

38. What are the unique challenges for emerging and developing economies in meeting the requirements of the transition to a net zero and nature-positive global financial system, and how can the UK best provide support to overcome these?
FIA EPTA decided not to answer this question.

Mobilising finance in emerging and developing economies using green bonds

Questions

39. Considering the key market incentives and barriers, how can the UK best support an increase in high quality, green bond issuances for emerging and developing economies?
FIA EPTA decided not to answer this question.