ACCELERATING CLIMATE ACTION IN THE BOARDROOM

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Boards, independent directors and senior management play a critical role in the climate transition as they steer and oversee their organisation's climate strategy, governance, risk management and transition planning. Climate governance has been a key pillar of the EBRD's green strategy and is central to client engagement. As part of these efforts, the EBRD has been working with the Climate Governance Initiative since 2022 to improve the climate governance of companies and boost boards' capacity to move towards a net-zero economy in the EBRD regions.

INTRODUCTION

Climate change is a major disruptor of global business. Climate change-related risks, impacts and opportunities are unique, owing to distinct characteristics such as the need for long-term business planning, the high levels of uncertainty involved, the scarcity of historical data (inhibiting analysis of future trends) and the unprecedented impact on value chains. With growing pressure from regulators, financial institutions, consumers and other stakeholders to enhance climate action, boards and non-executive directors have broadened their focus beyond traditional corporate governance to include climate-related governance issues, climate risk and opportunity management, and the incorporation of climate considerations in their business model and strategy.

Various market developments and trends have accelerated this shift.

a) Focus on climate and sustainability-related disclosures

First, there is widespread consensus that climate and sustainability-related data are essential in order to monitor progress towards achievement of the goals of the Paris Agreement, the stated climate ambitions of countries under nationally determined contributions (NDCs) and climate commitments at corporate level. This, coupled with concerns about the impact that unmanaged climate-related risks could have on markets' financial stability, has triggered a wave of mandatory regulatory requirements and voluntary market-driven standards that require entities to identify, assess, manage and report on climate and sustainability-related matters. Clear and robust governance mechanisms, future-proof strategies, science-based targets and risk management mechanisms are at the core of those emerging standards.

For example, the Task Force on Climate-related Financial Disclosures (TCFD) emphasised governance as a building block of effective climate risk and opportunity management.[1] Governance is one of the four foundational pillars of the TCFD's recommendations. Subsequent sustainability disclosure standards have also followed this approach. The standards issued by the International Financial Reporting Standards Foundation's International Sustainability Standards Board (ISSB) – which the G20 recognises as a global baseline for sustainability-related disclosures – explicitly set requirements for a reporting entity's governance. Similarly, governance is one of the fundamental pillars of the European Sustainability Reporting Standards (ESRS), which are applicable to companies that fall within the scope of the EU's Corporate Sustainability Reporting Directive.

From a governance perspective, the TCFD recommendations, the ISSB standards and the ESRS all require disclosures relating to a board's oversight of climate-related risks and opportunities, as well as skills and competencies in respect of climate and sustainability-related decision-making. The ISSB standards and the ESRS, in particular, require the disclosure of an entity's climate transition plan, which is the action plan adopted by an entity to address climate-related risks, impacts and opportunities. The ESRS go a step further and require a reporting entity to disclose whether the transition plan has been approved by its management and supervisory bodies.

1 See World Economic Forum (2019).

Therefore, the prevailing disclosure regulations and standards implicitly place a responsibility on the management and supervisory bodies of an entity to effectively oversee, identify and manage climate related matters by requiring the disclosure of such internal governance arrangements. This, in turn, requires that boards have the knowledge, skills and experience needed to effectively discuss and decide on climate-related risks, impacts and opportunities and develop climate-conscious strategies.

b) Greater interest in sustainable investment

Second, market appetite for sustainable investment has risen sharply in recent years alongside investor and lender demand for increased climate and sustainability-related disclosure. The term "sustainable investment" refers to investments that consider the impact of climate change and other environmental, social and governance-related (ESG) issues. The 2024 Morgan Stanley Sustainable Signals survey[2] finds that more than half of individual investors (54 per cent) plan to increase their sustainable investment in the coming year, and more than three-quarters of individuals (77 per cent) are interested in sustainable investing. Robust climate governance arrangements and high-quality disclosure of such arrangements can help companies to signal their climate resilience to investors, which will lead to enhanced access to finance through new instruments such as green bonds and sustainability-linked loans.

c) Risk of climate litigation directed at corporate officers

Third, litigation against company directors and senior management for their actions or perceived inaction on climate-related issues is growing. Such litigation is usually related to senior officers' duties to oversee, identify and consider material climate-related matters in the entity's day-to-day operations. These cases involve interpreting legal obligations under corporate and financial law to protect shareholders and investors. The objective of bringing such litigation is to disincentivise companies from continuing with high-emission activities or, in the case of the financial sector, to disincentivise investment in high-emission assets. Increasingly, courts are having to adjudicate on matters relating to private and public entities' handling of climate-related impacts and risks, so directors and senior officers will increasingly be expected to assume responsibility for their company's actions or inaction in relation to climate change.

2 See Morgan Stanley Institute for Sustainable Investing and Morgan Stanley Wealth Management (2024).

As directors are accountable to shareholders for their organisation's performance, they are increasingly being expected to address climate change and sustainability issues with the same level of scrutiny as any other issue posing a financial risk to the business. However, overseeing climate and sustainability-related matters presents new challenges for boards because of the significant uncertainty involved, the lack of historical data (which makes it difficult to accurately assess impacts, risks and opportunities) and the need to carry out forecasting in the absence of such data. Non-executive directors – sometimes also called independent directors – have a special role to play in holding management to account and asking difficult questions, and this now extends to matters pertaining to climate and sustainability risks, impacts and opportunities. In this context, it is interesting to note that in the 2024 EY Europe Long-term Value and Corporate Governance Survey,[3] fewer than 10 per cent of non-executive directors and chairs reported complete satisfaction with their companies' business rationale for sustainability.

3 See Teigland and Hobbs (2024).

4 See EBRD (2022).

THE EBRD'S ROLE IN PROMOTING CLIMATE AWARENESS IN THE BOARDROOM

Environmentally sound and sustainable development is central to the EBRD's mandate and is promoted through every project and policy initiative. The Bank has committed to becoming a majority green bank by 2025 and has met this commitment over the last two financial years. Since 1 January 2023, the Bank has fully aligned its activities with the mitigation and adaptation goals of the Paris Agreement.[4] Through policy reform and investment, the Bank also helps its clients and countries of operation to align their business models and economies with the goals of the Paris Agreement.

To enhance climate governance among senior managers of companies and financial institutions in its regions, the EBRD has established a dedicated Corporate Climate Governance (CCG) Facility. CCG refers to the set of rules, practices and processes that an entity puts in place to identify and manage the effects of climate change and improve decision-making and disclosure in relation to those impacts. The CCG Facility consolidates the policy reform and business advisory support that is provided by the

EBRD in order to help private-sector and state-owned entities to develop and strengthen their climate-related governance, strategy, risk management, target-setting and disclosure practices.

A key form of business advisory support offered to clients under the CCG Facility is support with developing and implementing corporate climate governance action plans (CCGAPs). Notably, the CCG Facility provides: (i) support with entity-level assessment of governance gaps in respect of climate issues; and (ii) capacity-building support to improve the entity's climate governance and disclosures, in accordance with international best practices and standards.

The Bank has developed policy products and partnerships for the benefit of corporate clients, financial institutions and other stakeholders, with donor support provided through the CCG Facility. For example, the Bank has a long-standing external nominee programme, through which it engages with a network of more than 100 non-executive directors on the boards of its investment companies. Under the CCG Facility, the EBRD has developed a climate toolkit in order to: (i) help its nominee non-executive directors to gain a robust understanding of the governance of climate-related risks, impacts and opportunities; and (ii) equip them with the tools and information they need to become strong drivers of climate action and sustainability in their respective companies. This toolkit helps non-executive directors to assess their company's climate governance maturity and outline the steps needed to strengthen the company's climate agenda.

Other directors and senior managers also have a critical role to play in the climate transition. Their engagement is vital for strategic guidance and oversight on climate action, as well as for the credibility of transition plans and organisational disclosures. However, effective fulfilment of this new role requires both organisational mandates and capacities that are often lacking, especially in emerging markets. In the 2022 Boston Consulting Group-INSEAD Board ESG Pulse Check,[5] around 70 per cent of directors reported that they were only moderately effective or not at all effective at integrating sustainability into company strategy and governance. Among companies with a net-zero commitment, only 55 per cent of directors reported that their organisation had prepared and published a plan for meeting that target.

The actions of private and public-sector entities in the EBRD regions are crucial not only for addressing the climate crisis but also for building strong and resilient economies.

Looking specifically at the EBRD regions, several economies are particularly vulnerable to climate and sustainability risks. This stems from a combination of factors, including geographical characteristics and historical under-investment, which has resulted in infrastructure that is significantly exposed to the physical impacts of climate change. At the same time, there is a significant lack of awareness in these markets and a lack of readiness to effectively identify, consider and mitigate climate-related risks or leverage climate-related opportunities. Many companies in these economies still do not adequately consider the risks associated with the physical impacts of climate change and the transition to low-carbon economies when making business and investment decisions.

The actions of private and public-sector entities in the EBRD regions are crucial not only for addressing the climate crisis but also for building strong and resilient economies. Supporting directors and senior management on their climate journey can help to reduce the climate risk exposure of the EBRD's investments. This support is also vital to achieve the Bank's objective of greening its economies. To increase its impact beyond its projects and clients, the Bank has been working with the Climate Governance Initiative (CGI) on the Chapter Zero initiative since 2022, supported by the CCG Facility.

5 See Boston Consulting Group and INSEAD (2022).

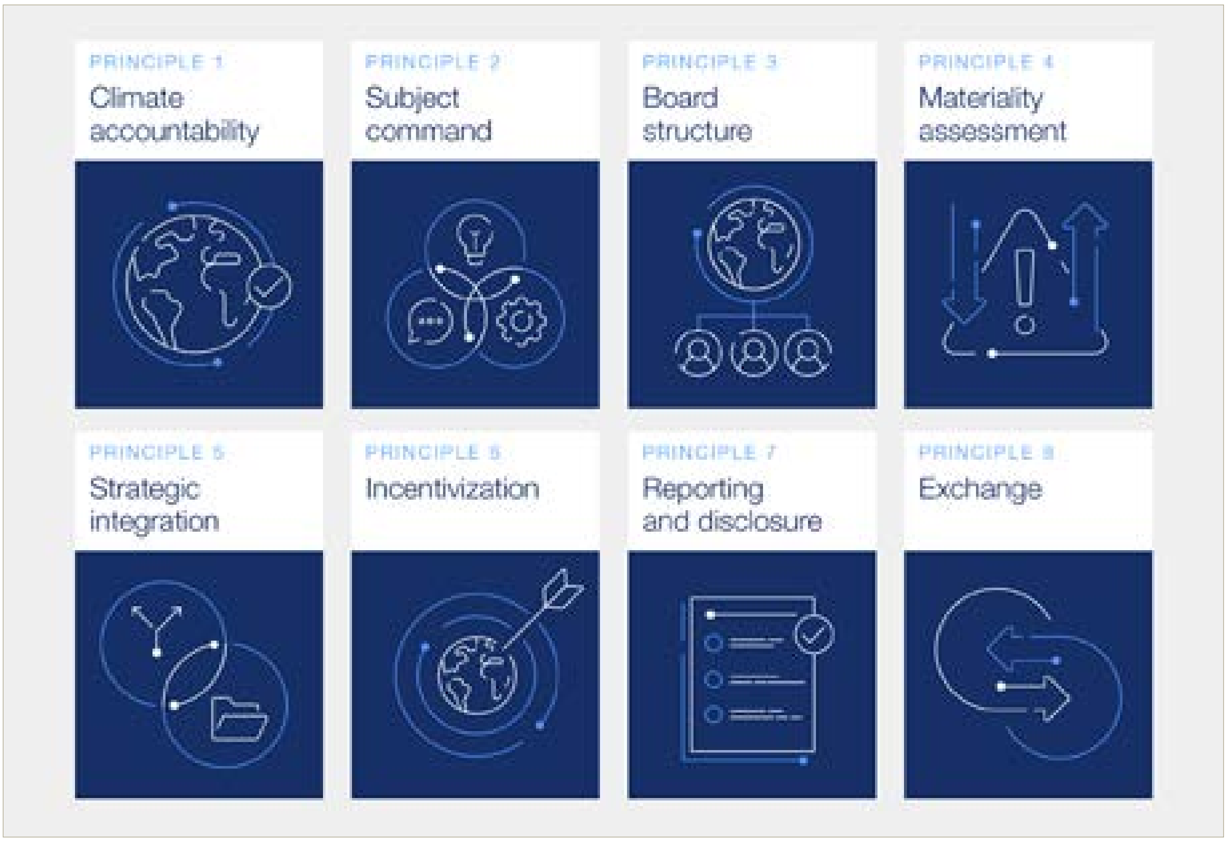
> The EBRD's partnership with the Climate Governance Initiative aims to help senior management of companies and financial institutions in the EBRD regions to improve their capacity to identify and address climate risks, impacts and opportunities, carry out transition planning and prepare climate disclosures.

THE EBRD'S PARTNERSHIP WITH THE CGI

The EBRD's partnership with the CGI aims to help senior management of companies and financial institutions in the EBRD regions to improve their capacity to identify and address climate risks, impacts and opportunities, carry out transition planning and prepare climate disclosures. The CGI was conceived in 2019 as a result of work by the World Economic Forum (WEF) focusing on climate action in the corporate world. It helps companies to set a climate target and develop a plan to meet it.

The foundation of the CGI's work is the WEF's eight Principles for Effective Climate Governance (see Figure 1),[6] which range from board accountability (to ensure long-term resilience to climate risk) to knowledge exchange (keeping informed through dialogue with investors, policymakers and others). These principles build on existing corporate governance frameworks such as the International Corporate Governance Network's Global Governance Principles, as well as other climate risk and resilience guidelines, including the recommendations of the TCFD.

Figure 1. The World Economic Forum's eight Principles for Effective Climate Governance



Source: World Economic Forum (2019).

6 See Climate Governance Initiative (2019).

The CGI launched Chapter Zero in 2019 in order to mobilise and educate directors and equip them with the skills and knowledge needed to address climate change at board level by applying the WEF's Principles for Effective Climate Governance.

CHAPTER ZERO IN THE EBRD REGIONS

The EBRD has worked closely with the CGI and local host organisations to launch five Chapter Zero organisations – referred to as "chapters" – in Egypt, Kazakhstan, Türkiye, Ukraine and the Caucasus, and Uzbekistan.

Each chapter is set up as a network of boards, non-executive directors and senior managers who are working towards integrating climate risks and governance into the overall business strategy of their entity. It is designed as a platform enabling chapter members to exchange their organisation's practical experience of managing climate-related governance risks, and strategies. Members of those chapters can learn from experts and peer companies that are advanced in the area of climate action in their respective countries by participating in knowledge-sharing events. Chapter members also have access to expert knowledge on climate-related risks, impacts, opportunities and strategies acquired by more advanced chapters, as well as access to leading consultants through webinars, training sessions and workshops organised with the support of the EBRD and the CGI.

Box 1. **Chapter Zero Egypt**

"Chapter Zero Egypt exemplifies the power of collaboration and proactive engagement in addressing climate challenges.

As the first initiative of its kind in Africa and the Middle East, it sets a commendable precedent for fostering climate-resilient business practices. This pioneering initiative marks a significant milestone in climate governance in the region.

As we emphasise the important role of the private sector in climate action, this platform provides invaluable resources and collaboration opportunities for business leaders, allowing them to navigate towards sustainable and low-carbon models. The EBRD is proud to support Chapter Zero Egypt and looks forward to it playing a pivotal role in promoting climate-conscious decision-making among business leaders in Egypt."

Khalid Hamza, Former Head of Egypt, EBRD

Members of those chapters can learn from experts and peer companies that are advanced in the area of climate action in their respective countries by participating in knowledge-sharing events.

For example, Chapter Zero Egypt,[7] which was officially announced at the United Nations Conference of the Parties (COP27) in Egypt, has organised awareness-raising webinars for members on a wide range of topics – including carbon credits, sustainability disclosures, ESG reporting guidelines and the development of sustainability strategies. Chapter Zero Egypt is thereby supporting the green transition of the private sector in the region (see Box 1). Similarly, Chapter Zero Türkiye has organised, in collaboration with the Turkish Industry and Business Association (TÜSİAD), panel discussions and round tables with C-suite executives on the topic of industrial decarbonisation and navigation of the climate challenge at company level.

In some emerging-market economies, an additional challenge may lie in the corporate governance practices of the market, which need to be taken into account when framing the support offered by the chapter. In Uzbekistan, for example, the EBRD's *Corporate Governance in Transition Economies* report[8] revealed a significant lack of corporate governance awareness across the business community, identifying weaknesses in areas such as transparency, disclosure, and the structure and functioning of the board. Clear governance structures and independent boards with strong mandates are important in order for directors and senior management to address climate and sustainability matters effectively.

3 See www.dailynewsegypt.com/2023/10/03/chapter-zero-launched-activities-in-egypt-in-september-2023

4 See EBRD (2020).

Box 2. **Chapter Zero Uzbekistan**

"Collaboration with Chapter Zero in EBRD countries of operation is an opportunity to engage with highly professional, motivated, proactive and self-driven country leaders who are at the forefront of sustainability and business development action in their communities. It is they who drive local change, paving the way to a better and more sustainable future. Supported by international experience and leveraging their own multifaceted complementary expertise and extensive local networks, chapter members are uniquely placed to make meaningful improvements in their countries.

One example of such cooperation was the development by Chapter Zero Uzbekistan of the Corporate Governance Handbook. This idea came from local chapter members, who accurately identified the market gap. Indeed, before introducing corporate climate governance to local firms and building their capacity to respond to climate risks and opportunities, it is necessary to enhance corporate governance in general. To this end, chapter members with extensive experience in this area have been resolute in driving the development of the Corporate Governance Handbook for Uzbekistan.

The EBRD has accumulated a wealth of experience in this area through many projects reforming the governance of state-owned enterprises and enhancing governance structures. With input from representatives of four EBRD departments, the chapter delivered a comprehensive guide tailored to the local context. The chapter's host institution, Westminster University in Tashkent, skillfully managed and supervised the material and its delivery to ensure that the final product was coherent, satisfied market needs and met businesses where they are.

This was a very rewarding experience, and we look forward to carrying out more meaningful action in local markets together with Chapter Zero members."

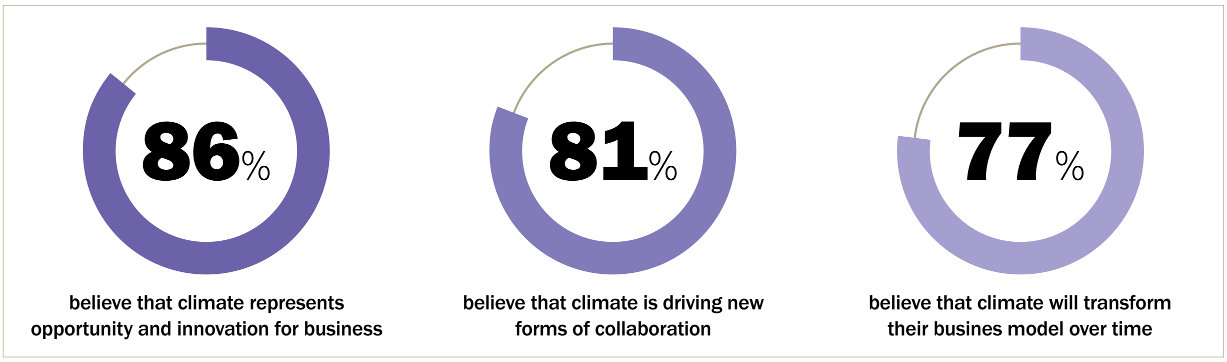
Solomiia Petryna, Principal, Green Financial Systems team, EBRD

As these economies shape their governance landscapes, there is an opportunity to integrate climate governance principles while advancing corporate governance practices, adopting a forward-looking approach that prioritises climate considerations within corporate governance. The EBRD, with its considerable expertise in corporate governance and climate-related practices, is well placed to support its clients on this, as it has in the case of Chapter Zero Uzbekistan (see Box 2).

Last year, the CGI partnered with Kantar to conduct a Global Impact Study covering all Chapter Zero initiatives,[9] which concluded that the more a board director engages with their local CGI chapter, the more likely they are to take positive action in climate discussions in the boardroom. The report also revealed a clear need for Chapter Zero support: nine out of ten respondents said that the climate challenge required new forms of leadership from boardrooms.

[9] See www.chapterzeroslovenia.si/en/knowledge-hub_1/global-impact-study-findings-2024-how-can-we--advance-climate--action-on-boards/

Figure 2. Encouraging findings from the Global Impact Study conducted by the CGI and Kantar



Source: Climate Governance Initiative and Kantar (2024).

CONCLUSION

Advancing climate governance and climate action within the boardroom is a strategic imperative for modern businesses. As companies begin their climate journey, it is crucial to build awareness of climate and sustainability-related risks, impacts and opportunities, while understanding the evolving market and regulatory expectations. For those that are more advanced in terms of sustainability efforts, systematically integrating climate considerations into core business processes is essential.

Support provided through the EBRD's CCG Facility – including the Chapter Zero initiatives – seeks to ensure that all companies, regardless of their maturity, size and sophistication, are aligned with the goals of the Paris Agreement and adhere to internationally recognised standards or local regulations. By integrating sustainability considerations into decision-making, boards can drive a systematic greening of their companies, suppliers and economies. Ultimately, robust climate governance and proactive climate action will pave the way for sustainable growth and resilience, positioning companies as leaders in a rapidly changing global landscape.

Advancing climate governance and climate action within the boardroom is a strategic imperative for modern businesses. As companies begin their climate journey, it is crucial to build awareness of climate and sustainability-related risks, impacts and opportunities, while understanding the evolving market and regulatory expectations.

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