

1 December 2023

## **Sustainable finance consultation: MQBS & Cyan Ventures joint submission**

### **Introduction and context**

Thank you for inviting consultations to the Treasury's sustainable finance consultation. Macquarie Business School (MQBS) is one of the leading sustainability policy research schools in the country and is being supported by Cyan Ventures - a new sustainability consulting and project development firm that is focussed on accelerating the deployment of sustainability technologies at 3-5x faster than the current pace.

We welcome Treasury's focus on the area of sustainable finance as it is vital to the energy transition and an area which has until recently had insufficient attention. We also believe that the areas of transparency, capability and leadership are critical elements of a sustainable finance strategy that require improvement.

Three additional overall considerations would strengthen the sustainable finance strategy:

1. **Taking an integrated approach to sustainable finance and establishing Australia's leadership.** The strategy should provide an overarching view of Australia's role in the energy transition, the place of sustainable finance and integrate social and environmental aspects together
2. **Improving transparency but without onerous reporting.** A labelling scheme would be helpful but should start with simple input metrics – ultimately outcome metrics such as emissions reduction over time might be appropriate
3. **Developing equitable financial incentives for renewables for consumers.** The capacity investment scheme will assist with large scale renewables; consumers and businesses should not be left out, particularly those with less financial resources

This short note takes each of these points in turn. More detailed points in response to the consultation are found in the Detailed Submission that follows in Appendices B-C.

### **1. Taking an integrated approach to sustainable finance and establishing Australia's leadership**

A sustainable finance strategy is only as effective as the overall energy transition strategy and the degree to which economic incentives are linked up across the economy. While we recognise this consultation is focussed on key regulatory enablers, inevitably a sustainable finance strategy needs to answer questions such as:

- What are Australia's comparative advantages as a nation in the energy transition?
- What is the strategy or lowest cost / most feasible way of using these advantages through the energy transition?
- What role does sustainable finance play in supporting Australia to achieve the above two objectives?
- In a context where it may not be possible to apply a single carbon price across the economy, what does an integrated approach to sustainable finance consist of?

Currently, the overall approach to the energy transition is reflected across a range of policies, regulations and institutions<sup>1</sup> which makes it incredibly difficult to understand, let alone manage the transition as a whole. There is, as yet, limited shared understanding of Australia's unique contribution to the energy transition nor a clear viewpoint of the lowest cost / least risky pathway to achieving that transition. Practically, the result is a set of carbon prices that are applied unequally across the economy; with governments arbitrarily "picking winners" across the economy. This translates into a complex framework for sustainable finance as well; the strategy is piece-meal with a mix of regulatory niches with limited transparency on where funds are flowing (e.g. limited large fund investment into renewables). Our overall recommendation is that there needs to be a clearer objective(s) with fewer simple policy levers. This would then flow through to clearer sustainable guidelines that would provide the private sector and consumers sufficient clarity and incentives to play their role.

An overall strategy also needs to be integrated across key environmental and social objectives. An example of how a sustainable finance strategy could take an integrated approach is with biodiversity. It makes sense to develop frameworks which integrate climate, nature, and social aspects to capture the relevant externalities together. A specific example is bundled carbon and nature markets. An example of a specific integrative approach is the development of extended markets for carbon dioxide permits (or units) which can be bundled with biodiversity credits (NSW Government, 2022) and distributed via recurrent auctions. This approach provides a price incentive to guide production and consumption decisions which affect both the climate and nature. It can fast-track attempts to price nature where inherent challenges for measuring nature can prevent a successful stand-alone market. Future auctions can incorporate improved measurement of nature over time. Appropriate use of auction revenues may be crucial for public support (Klenert et al., 2018), despite potential trade-offs with economic efficiency.

## **2. Improving transparency in sustainable finance but without onerous regulation**

Transparency is critical to an effective sustainable finance approach. One of the key issues associated with current climate initiatives has been the gap between ambition and action. Analysis by MQBS suggests mixed results on the relationship between disclosures and sustainability performance, especially when disclosures focus on qualitative information related to process, strategy, initiatives, that together may not lead to the desired performance outcomes, see, e.g. Bui, Chelli, and Houque (2022), Anetsmann, Trück, and Wilkens (2023). Both studies suggest that firms may increase their disclosure scores symbolically while not being motivated to reduce their emission performance. It is critical to provide firms with incentives, and pressures, to align disclosure with actual performance improvement.

At the same time, many companies and financial institutions have recruited large ESG teams which spend much of their time reporting on a range of ESG metrics. There needs to be the right balance between transparency and regulatory burden so that only the key metrics are captured.

A sustainable finance labelling system would improve transparency. However, labelling relies on very simple answers to complex questions. "Sustainability" is extremely hard to define with many possible interpretations of what "sustainability" is. For example, our internal research shows ESG sustainability ratings are uncorrelated suggesting that there is no single "sustainability" metric.

The EU has significant guidance on this topic, for instance at the EU level there have been suggestions of minimum investment in sustainable assets; pursuit of a sustainable investment strategy or

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<sup>1</sup> At the Federal level alone, some of the key policies include: SafeGuard Mechanism, Capacity Investment Scheme, Rewiring the Nation, Electric Vehicle Policy, Hydrogen Head Start orchestrated by a range of agencies, DCCEEW, PM&C, Treasury, CEFC, ARENA, National Reconstruction Fund, NZEA, CCA. States have a similar level of complexity.

replication of a sustainable index. Our view is that a simple approach in the first instance is warranted, something similar to the UK's suggested approach that focusses on input metrics:

- **Transitioning** - sustainable characteristics, themes or objectives; low allocation to Taxonomy-aligned sustainable activities
- **Aligned** - sustainable characteristics, themes or objectives; high allocation to Taxonomy-aligned sustainable activities
- **Impact** - objective of delivering positive environmental or social impact

Eventually output or outcome focussed metrics should be the goal; with levels of decarbonisation to industry benchmarks a possible.

The role of the government should be light touch. A voluntary labelling approach for sustainable investments is worth trying rather than “regulating ESG ratings”. A voluntary approach has been used for the Health Star Rating system<sup>2</sup>. There is an opportunity for existing or new organisations to provide more detailed numerical ratings on investment sustainability. Existing organisations already consider relevant issues in their ongoing research.

Another option to consider is defaults. The challenge of incorporating views of individual superannuation investors into strategies for sustainable investment is a lack of engagement from many people. Succinct labelling mentioned above is crucial in this low-engagement context. Where individuals still avoid making active investment decisions, the setting of default investments is important. Consideration can be given to using sustainable investment options as defaults, especially for investor types who are more likely to show low interest.

Other key aspects related to taking an integrated approach and improving transparency in sustainable finance, where MQBS has strong expertise are outlined in Appendix B and relate to carbon assurance to address greenwashing, see, e.g. Luo, Tang, Fan, and Ayers (2023), an appropriate corporate governance framework, see, e.g. Liao, Luo, and Tang (2015), Luo and Tang (2021), Choi and Luo (2021), the timing of the reporting mandate, see, e.g. Moses, Bui, Houqe and Borghei (2023) as well as supporting capacity building in disclosures for Australian firms, see, e.g., Borghei, Linnenluecke, and Bui (2023) and sustainable lending and investment, see, e.g., Smith, Linnenluecke, Liao, Bu (2022-2024 ARC Linkage Grant).

### 3. Developing equitable financial incentives for renewables particularly for businesses and households

Recently, the most immediate practical challenge for the government has been to incentivise renewable development in Australia. Australia has been off-track to hit its 82% renewable goal by 2030.<sup>3</sup> Major super funds have not invested significantly in Australia with planned renewable investment slowing since 2020. Many of the large solar projects that were commissioned over the last 5 years are currently being restructured as they are no longer commercial. There is also significant regulatory risk associated with these projects.

The recent announcement of the expansion of the capacity investment market is positive and will likely address a significant part of the existing gap. But there continue to be issues deploying these renewables such as permitting, skills, and transmission that require resolution. There is also concern about the undocumented cost of the expansion of this scheme.

<sup>2</sup> <https://www.foodstandards.gov.au/consumer/labelling/Pages/Health-Star-Rating-System.aspx>

<sup>3</sup> <https://www.afr.com/companies/energy/long-haul-ahead-to-right-off-track-energy-transition-20231011-p5ebix>

Most importantly, there is a need for further support for households and businesses to also invest in behind the meter renewables. Arguably the most successful element of Australia's energy transition today has been the consumer take-up of roof-top solar with over 30% of households in Australia being able to use over 14 gigawatts (APVI, 2023). As the energy grid moves from a centrally planned to a decentralised system it will be important for consumers / small businesses to play an important role. The right incentives for consumers to adopt rooftop solar and batteries can reduce power bills and further address cost of living challenges. This will also require new sustainable finance mechanisms that allow for this take-up.

A key principle for designing incentives for household energy investments like solar panels is that incentives differ according to ability to pay. Otherwise, wealthy households will receive greater incentives than they require, while some less wealthy households will still be unable to access energy investments. Inequality may grow further, such as between homeowners and renters and within the renter group (Best and Chareunsky, 2022; Best, Chareunsky and Taylor, 2023). More precise means testing is crucial, including reference to household assets rather than just income (Best and Chareunsky, 2022).

An innovative way to achieve greater precision in policy targeting would be an equitable reverse auction for incentives (Best, 2023). Equitable reverse auctions would open a new market where the government is a buyer of social benefits such as emissions reduction. Governments could offer a range of support types, such as rebates for electric vehicles. Households would cover the balance of costs, leading to co-investment. Further detail is provided in Appendix C.

Please see the appendices for details about the sustainability capabilities of Macquarie Business School and Cyan Ventures (Appendix A), financial disclosures (Appendix B), and integrated approaches to incentivising sustainable investments (Appendix C).



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## Appendix A: MQBS & Cyan Ventures Capabilities in Sustainable Finance

**Macquarie Business School (MQBS)** has expertise in researching sustainable solutions to pressing environmental and social problems, providing evidence-based strategies to address environmental and social change. Our expertise across various Departments, disciplines and Centres includes:

***Transforming Energy Markets (TEM) Research Centre:*** The TEM Research Centre promotes world-leading interdisciplinary research that facilitates the smooth transition of existing, emerging and new energy markets to a decarbonised future. For energy market stakeholders and decision-makers, this involves sustainable finance and technology solutions for the structure of wholesale electricity markets; the creation and design of new markets such as carbon credit units; and the sustainable integration of new energy sources and technologies into the energy system.

<https://www.mq.edu.au/gem/research-centres-facilities-groups/centres/transforming-energy-markets>

Contact: Professor Stefan Trueck, Director [stefan.trueck@mq.edu.au](mailto:stefan.trueck@mq.edu.au)

***Smart Green Cities (SGC) Research Centre:*** The Smart Green Cities Research Centre develops collaborative evidence-based solutions for liveable smart green cities of the future. This cross-Faculty Centre, led by the Faculty of Science and Engineering, brings together world class expertise in green and blue infrastructure; smart technologies and sustainable cities.

<https://www.mq.edu.au/research/smart-green-cities>

Contact: smartgreencities@mq.edu.au, Prof Michelle Leishman, [michelle.leishman@mq.edu.au](mailto:michelle.leishman@mq.edu.au) and Dr Rohan Best, SGC Executive [rohan.best@mq.edu.au](mailto:rohan.best@mq.edu.au)

***Sustainability / environmental accounting:*** We are at the forefront of efforts to understand, measure, manage, and transparently report carbon emissions and other climate related information, as well as to navigate and address the complexities and dynamic nature of climate change-related practices and impacts. We leverage the combined expertise, innovations, ideas, and solutions from industry and academia to serve, support, and enable various stakeholders, including industries, government and regulatory bodies, and communities. We act as a hub for knowledge exchange, capacity building, and practical solutions, contributing to the collective efforts towards a more sustainable and environmentally conscious world.

Contact: A/Prof Laura Le Luo, [le.luo@mq.edu.au](mailto:le.luo@mq.edu.au)

***Climate Finance:*** We investigate novel approaches for advancing ecological sustainability via financial mechanisms. Our approach involves the integration of financial mechanisms and behavioural nudges to incentivize individuals and corporations to adopt environmentally sustainable practises. Our research endeavours encompass the examination of sustainable lending via credit scoring that incorporates carbon footprints, the analysis of the effects of banks offering customised carbon footprint feedback, and the facilitation of sustainable investing education to empower retail investors.

Contact: A/Prof Di Bu [di.bu@mq.edu.au](mailto:di.bu@mq.edu.au)

***Corporate Sustainability and Environmental Finance:*** An interdisciplinary team of leading experts in strategy, finance and sustainability researching how organisations' strategic decisions, investment choices and the uptake of sustainable finance can help to tackle some of the world's most

pressing environmental and social problems including climate change and resource depletion.  
Contact: A/Prof Abhay Singh [abhay.singh@mq.edu.au](mailto:abhay.singh@mq.edu.au)

### **Cyan Ventures**

Cyan Ventures is an advisory and project development company, focused on accelerating the deployment of sustainability technologies at 3-5x faster than the current pace. We do this with an inter-disciplinary team of leading strategists, project developers, and researchers. Cyan Ventures is being led by Shaun Chau and Dr Fraser Thompson.

Shaun was former head of sustainability at Accenture, as well as part of BCG's Energy and Renewables leadership team in Europe. He was previously part of the leadership team of the Tony Blair Institute and started his career at No.10 Downing St. He has a masters in public policy (Oxford) and arts / law degree from UNSW.

Fraser holds a PhD in Economics from Oxford University (Rhodes Scholar), was a lecturer in economics at Oxford University and economist at the World Bank. He spent 9 years at McKinsey & Company, including leading McKinsey Global Institute (MGI) on sustainability topics globally. He was recently co-founder of Sun Cable, the world's largest solar farm in the Northern Territory.

Contacts: [shaun.chau@cyanventures.com.au](mailto:shaun.chau@cyanventures.com.au); [fraser.thompson@cyanventures.com.au](mailto:fraser.thompson@cyanventures.com.au)



## **Appendix B - Additional Key Aspects Related to Taking an Integrated Approach, Establishing Australia's Leadership and Improving Transparency in Sustainable Finance**

### **Carbon Assurance to Address Greenwashing**

Assurance plays a pivotal role in sustainable finance by enhancing the credibility and reliability of sustainability disclosures. The importance of assurance lies in instilling confidence in stakeholders, fostering trust, and supporting informed decision-making. It helps companies demonstrate their commitment to sustainability, mitigates the risk of greenwashing, and contributes to the overall integrity of sustainable finance initiatives. Ultimately, assurance is a critical component for building a robust and transparent foundation for sustainable finance practices. Tang (2019) demonstrates that carbon auditing functions as a tool for managing transitions and governing sustainable socio-technical and organizational innovation and transformation. Fan, Tang, and Pan (2021) also highlight that resolving carbon information asymmetry requires carbon assurance, which cannot be substituted for by financial auditing. Luo, Tang, Fan, and Ayers (2023) uncover that companies that adopt carbon assurance tend to have better carbon disclosure quality in the subsequent year than their unassured peers.

In light of these findings, several key recommendations emerge to enhance the effectiveness of sustainability assurance practices to promote transparency within the context of sustainable finance:

- Implement and enforce standardized assurance frameworks for sustainability disclosures. Develop clear guidance outlining the roles, responsibilities, and qualifications of assurance providers to ensure consistency and reliability in the assurance process.
- Invest in educational programs to enhance the capacity and expertise of sustainability reporting and assurance professionals. This includes training initiatives, certifications, and ongoing professional development to keep practitioners abreast of evolving sustainability reporting standards.
- Collaborate with international standard-setting bodies to align national assurance practices with global best practices. This ensures that assurance processes are internationally recognized and harmonized.
- Leverage technology, such as blockchain or advanced data analytics, to streamline and enhance the efficiency of assurance processes. Explore innovative solutions that can improve the accuracy, timeliness, and cost-effectiveness of sustainability disclosure verification.
- Consider involving independent third-party verification or certification bodies to assess and verify the adherence of investment products to sustainability criteria. This adds credibility and ensures that the labelling process is rigorous.

### **An Appropriate Corporate Governance Framework**

Corporate governance (CG) and the role of the board of directors play a pivotal role in ensuring sustainable finance within companies. Liao, Luo, and Tang (2015) investigated the impact of corporate board characteristics on the voluntary disclosure of greenhouse gas (GHG) emissions within a sample of UK firms. Their findings reveal that boards characterized by greater gender diversity, a higher proportion of independent directors, or the presence of environmental committees are more inclined toward embracing sustainability transparency. However, the effectiveness of these committees is contingent on factors such as size, independence, and activity level. Similarly, Luo and Tang (2021) reveal a tangible impact of overall CG quality on carbon performance and identifies that the relationship between CG and carbon performance is notably influenced by carbon strategy and



managerial awareness of carbon risk. Choi and Luo (2021) document that firms with robust corporate governance structures are perceived more favourably by shareholders in terms of their ability to manage carbon-related risks. These results emphasize the importance of robust corporate governance frameworks in driving sustainability practices. Recognising this, governments can take strategic steps to reinforce corporate governance practices and empower boards to drive sustainable initiatives. Here are key recommendations:

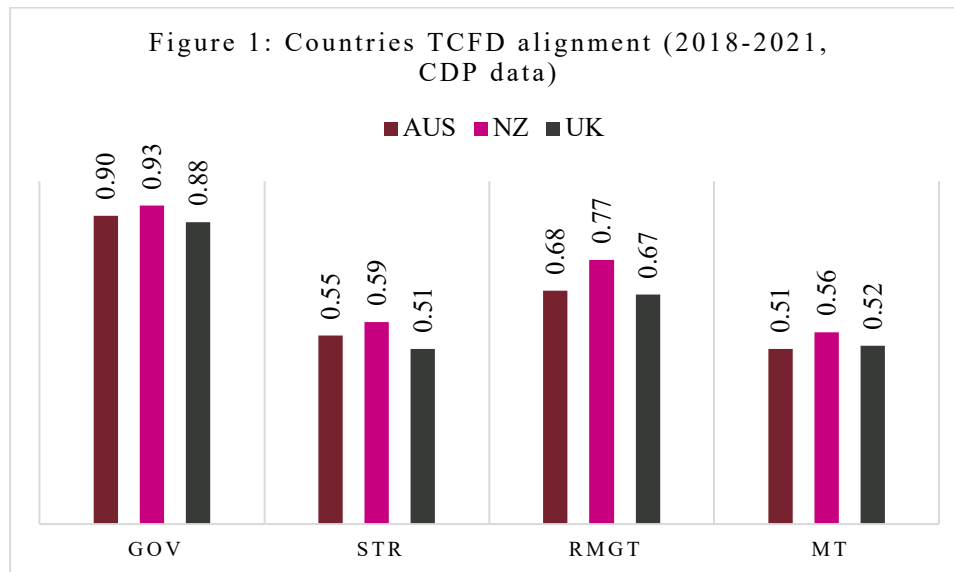
- Encourage or mandate diversity on boards, including expertise in sustainability matters. Diverse boards bring a range of perspectives, fostering more comprehensive decision-making on sustainability issues.
- Encourage the formation of dedicated ESG committees within boards to focus on sustainability matters. These committees can provide specialised attention to ESG issues, ensuring a more focused approach to sustainable finance.
- Establish requirements for ongoing education on sustainability matters for board members. This ensures directors are equipped with the knowledge and understanding needed to effectively navigate and oversee sustainability challenges.

### ***The Timing of the Reporting Mandate***

The Task-Force on Climate-Related Financial Disclosures (TCFD) recommends disclosures for the largest listed and unlisted companies and financial institutions to start on 1 July 2024, with other companies being phased-in over time. This approach has only taken into account the risk aspect of sustainable finance, with large companies and financial institutions being well-placed to make a considerable impact on the movement towards a low-carbon finance system. However, this fails to take into account the differential capacity within an organisation regarding different aspects of TCFD recommended disclosures. The UK government has proposed the adoption of a phased-in approach with compliance (Phase 1), risk management and targets and metrics (Phase 2) and strategy (Phase 3). Similarly, the New Zealand Government proposed provisions for strategy disclosures, particularly relating to transition planning and scenario analysis. A recent MQBS research study compares the preparedness of firms in the UK, Australia and New Zealand to comply with TCFD recommended disclosures, using CDP data. The findings of the study provide support for this phased-in component-driven approach whereby there are significant variations in firms' preparedness to comply with TCFD disclosures across the four components, with strategy, targets and metrics lagging behind in terms of reporting quality (see Figure 1).

Hence, we propose that the Government considers a phased-in component-driven approach with compliance required firstly for Governance, followed by risk management, and lastly, metric, targets and strategy.

Further, Figure 1 also shows that Australian firms are comparable to UK firms in terms of reporting preparedness, while lagging behind New Zealand firms. Consequently, we argue that a mandate on Australian firms to provide TCFD recommended disclosures should not cause disproportionate compliance cost, especially for largest listed firms.



Source: Moses, Bui, Houque and Borghei (2023)

We propose Australian Government should mandate TCFD recommended disclosures as early as possible, to align with global developments, e.g. the UK and New Zealand.

### ***Supporting Capacity Building in Disclosures for Australian Firms***

Based on MQBS research, we propose the following measures aiming at improving Australian firms' capacity in sustainability and climate-related reporting:

- The government provides training for firms regarding how to develop systems and capabilities regarding Strategy, and Metrics and Targets.
- To provide cross-industry collaboration and networking to develop best practices regarding TCFD-recommended disclosures; firms that have scored well in TCFD-recommended disclosures, especially due to past experience with CDP, can provide insights and advice to industry peers.
- The training and other support can be directed particularly towards emissions-intensive sectors due to their higher emissions risk and lower reporting preparedness.
- The government should investigate the potential to develop industry-specific metrics and industry-specific provisions, especially regarding transition planning and scenario analysis.

Besides the TCFD-recommended disclosures, it is increasingly pertinent that firms disclose climate-related financial risks in their financial statements. Following IASB's Climate-Related Disclosure Standards, another study (Borghei et al 2023) based on FTSE firms (2016-2020) show that the quality of disclosing climate-related risks in the annual reports and notes is low and inconsistent. Further, there are significant variations across the items, with fixed asset accounts being the most common impacts disclosed, with financial instruments and revenue-related accounts lagging. Particularly, while many firms commit to Net zero targets, they rarely quantify the financial impacts of the transition and the achievement of these targets. Additionally, high-emitting industries undertake a risk-based approach to the disclosure due to the particularly high-risk exposure to climate issues while low-emitting industries employ an opportunity-focused disclosure approach (Borghei et al 2023).

Based on our research, we recommend the following measures:

- The Government should acknowledge this potential reporting bias in financial statements between high and low-emitting industries whereby high-emitting industries follow risk-based and low-emitting industries follow an opportunity-based disclosure. Accordingly, the Government can provide guidance for each industry accordingly and/or issue guidance to ensure comparability and minimize selective disclosures.
- The government should particularly allocate resources to provide guidance and training on scenario analysis and quantifying the impact of the transition plan towards net-zero targets in the financial statements.

### **Sustainable lending and Investing**

Financial lending and investing also plays a crucial role in forming small businesses and households' sustainable decision-making and daily low-carbon behaviours. By directing investors' capital toward environmentally sustainable projects, advocating for responsible investment practices, and integrating climate risk assessments, the socially responsible investment (SRI) can significantly contribute to fostering a more resilient and sustainable future. According to the Global Impact Investing Network (GIIN), SRI investing has experienced rapid growth in recent years, with the current market estimated to be worth \$715 billion; however, retail investors still have limited access to the SRI investing. Bu, et al., (2022-2025) investigates the obstacles that impede retail investors from engaging in impact investing and provide interventions including sustainable trading education and green information disclosure to cultivate investors' green trading behaviour.

While sustainable investing has gained widespread attention among both scholars and practitioners, the concept of sustainable lending is now gaining momentum. This growing interest stems from the global quest to understand how bank loans and FinTech credits can impact the environmental performance of corporations and individuals alike, reaching a broader spectrum of economic activities and geographies, including public and private entities. However, despite extensive research on sustainable lending in the corporate banking sector, studies on sustainable lending in the consumer lending domain remain underdeveloped. Personalized carbon footprints are now accessible through banks and payment FinTechs, empowering individuals to monitor and comprehend their environmental impact. This development also presents an intriguing opportunity for the consumer lending industry to embrace sustainability-linked lending practices. Smith et al., (2022-2024) investigates whether the incorporation of an individual's environmental performance into consumer loan decision-making could create economic incentives to promote low-carbon activities.

For references, please refer to the main submission.

## **Appendix C – Further details on developing equitable financial incentives for renewables, integrated approaches, and labelling of sustainable investments**

### **Key points**

Two key points in general are:

1. Co-benefits beyond climate can be given more urgent and integrated attention.
2. Individuals and households can be more prominent in the strategy.

### **Context and problems**

1. A key principle in the Consultation paper is: “Efforts should begin with climate and progress to other environmental and social priorities” (p. 7, Consultation paper).

There are at least two reasons why delaying progress on other environmental and social priorities requires reconsideration. First, there is urgency in addressing issues such as biodiversity loss, due to irreversible impacts like species extinction [1]. Second, goals for climate, nature, and equity are connected [1]. Pursuit of one goal in isolation can worsen other priorities. For example, policy support for widespread adoption of solar panels by Australian households has helped for a sustainable climate transition, but has raised socio-economic inequality [2]. There is likely to be persistence or worsening in other specific forms of inequality, such as for First Nations people and renters [3], unless strategies consider key groups with specific policy formulation.

2. Another key principle is: “Collaboration and shared responsibility should be at heart of our approach .... [requiring] cooperation and partnership across community, business, investors and policymakers. Reforms to promote sustainable finance should be genuinely collaborative and consultative” (p. 7, Consultation paper).

#### *Greater focus on individuals and households*

Following this principle likely requires greater focus on individuals and households, relative to the current Sustainable Finance Strategy Consultation paper. The paper currently includes acknowledgement of various roles of individuals and households, such as roles as energy consumers and superannuation investors. Greater understanding of consumer and investor responses to frameworks and policies is required.

#### *Labelling for sustainable investments*

An important example is that labelling schemes for sustainable investment need to align with investor knowledge and preferences. Individual (retail) investors may not have a clear understanding of investment labels of “‘sustainable focus’, ‘sustainable improvers’ and ‘sustainable impact’” (Box 5; Consultation paper). A lack of investor understanding may then impact on investment behaviour.

#### *Policies for household upgrades*

There is also a lack of understanding on how individuals or households would respond to sustainable policy support. Some policies are too generous and receive a rush of applications while others are insufficient and receive very few [4], [5]. Over-generous funding exacerbates the problem of non-additional support [6], while insufficient funding raises inequality when only wealthy households can afford new technologies. This is relevant for the Household Energy Upgrades Fund (p. 33; Consultation paper).

## How problems can be addressed

In general, an experimental adaptive approach can be suitable for complex problems, like those discussed above. This would involve urgent action but with experimentation potentially motivating refinements to strategies and policies over time.

1. The problem of non-integrated approaches, such as climate strategies that omit nature and social benefits, is relevant for the Key principles on page 7 of the Consultation paper. It is also relevant for the feedback question in Priority 10 on “support[ing] financing and market development in areas with significant climate co-benefits, including nature and biodiversity”. The problem can be addressed with general and specific components.

### *General integrative frameworks*

The general component involves consideration of existing frameworks which integrate climate, nature, and social aspects. For example, one possible framework considers sustainable development goals while integrating climate, nature, and social aspects [7]. A general integrated perspective is useful to motivate specific approaches, as described in the next paragraph.

### *A specific example: bundled carbon and nature markets*

An example of a specific integrative approach is development of extended markets for carbon dioxide permits (or units) which can be bundled with biodiversity credits [8] and distributed via recurrent auctions. This approach provides a price incentive to guide production and consumption decisions which affect both the climate and nature. It can fast-track attempts to price nature where inherent challenges for measuring nature can prevent a successful stand-alone market. Future auctions can incorporate improved measurement of nature over time. Appropriate use of auction revenues may be crucial for public support [9], despite potential trade-offs with economic efficiency.

2. The problem of incorporating individuals and households into sustainable finance strategies and policies is relevant for Priority 4, 5, and 10 from the Consultation paper.

### *Simple starts, experimenting, and expanding*

The “key considerations for the design of a sustainable investment product labelling regime” (p. 21, Priority 4, question 1) should include usability of labels for investors. This is likely to be an empirical issue that requires experimentation. A good principle is to start with simple approaches and adjust over time. Some superannuation funds currently state actions such as “excluding companies generating more than 10% of their reported revenue from the extraction and production of thermal coal”<sup>4</sup>. One step for extension of these approaches is also prominently reporting statistics related to forestry, which is relevant for both climate and nature goals.

### *Food labelling to inform investment labelling*

The question of “how can an Australian model build off existing domestic approaches and reflect key developments in other markets?” (p. 21, Priority 4, question 2) can build from the simple start above. Domestic approaches in other fields might be relevant. Numerical aspects could be useful, as in food labelling with the Health Star Rating and Country-of-origin labelling<sup>5</sup>.

A voluntary labelling approach for sustainable investments is worth trying rather than “regulating ESG ratings” (p. 23, Consultation paper). A voluntary approach has been used for the Health Star Rating

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<sup>4</sup> <https://www.unisuper.com.au/investments/how-we-invest/responsible-and-sustainable-investing/climate-risk-and-our-investments>

<sup>5</sup> <https://www.foodstandards.gov.au/industry/labelling/pages/default.aspx>

system<sup>6</sup>. There is an opportunity for existing or new organisations to provide more detailed numerical ratings on investment sustainability. Existing organisations already consider relevant issues in their ongoing research.

### *Lack of engagement and defaults*

A challenge for incorporating views of individual superannuation investors into strategies for sustainable investment is a lack of engagement from many people. Succinct labelling mentioned above is crucial in this low-engagement context. Where individuals still avoid making active investment decisions, the setting of default investments is important. Consideration can be given to using sustainable investment options as defaults, especially for investor types who are more likely to prefer sustainable objectives [10]. It could then be appropriate that regular performance monitoring, which compares investment returns of superannuation funds, would separately consider sustainable and other funds.

### *Co-benefits from extra support beyond labelling*

Improved labelling alone is likely to be insufficient to achieve integrated goals for the climate, nature, and social outcomes. An additional component of an integrated strategy may include co-contributions or tax benefits for some superannuation investors. This could help with the social aspect of reducing the gender superannuation gap, which may be harder to reduce than the gender wage gap [11]. There may be opportunities for co-benefits in this context, if females are more likely to support sustainable investments [10].

### *Equity and sustainable finance flows and markets*

For question 1 of Priority 10 (p. 33, Consultation paper), a comprehensive approach to scaling up sustainable investment in Australia would consider equity to avoid inequitable past outcomes [2]. If support for households is not means tested, then it will likely lead to wealthier households being more likely to obtain newer energy technologies [2]. The Household Energy Upgrades Fund (p. 33; Consultation paper) should therefore have means testing as a central component of the strategy. An ambitious extension, which can be world-leading, is to use a newly-proposed approach of ‘equitable reverse auctions’ [12].

Equitable reverse auctions [12] would give a new market where the government is a buyer of social benefits such as emissions reduction. Governments could offer a range of support types, such as rebates for electric vehicles. Households would cover the balance of costs, leading to co-investment. For cost-effectiveness, the government would support the lowest rebate bids from households in a reverse auction context. However, this is likely to be inequitable, as households with more financial capacity would find it easier to submit low bids. Sub-auctions can therefore be run so households would be competing with others with similar economic characteristics.

Equitable reverse auctions could be used for supporting key groups such as renters and First Nations people. Greater assistance for renters also could indirectly help some First Nations people, given that First Nations people are more likely to be renters and that property rights are a large contributor to energy investment differences across demographic groups [13], [14]. Equitable reverse auctions to assist renters could be run for sub-groups of landlords, such that landlords could receive incentives for household energy upgrades that benefit renters. The sub-groups would be based on the socio-economic characteristics of the renters, such that more support would be provided to lower socio-economic renters.

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<sup>6</sup> <https://www.foodstandards.gov.au/consumer/labelling/Pages/Health-Star-Rating-System.aspx>



The reverse auction concept can also be extended in other ways. Other buyers could join this market, such as philanthropies or companies seeking to make voluntary contributions to emissions reduction or to obtain offsets for mandatory requirements in the future. Also, governments could extend the use of reverse auctions to more contexts, such as when providing support to small or medium businesses.

In relation to question 2 of Priority 10 (p. 33, Consultation paper), a key opportunity for the CEFC is in supporting sustainable investment in the above equitable manner.

A collaborative approach can be useful. This collaboration could include researchers, in addition to “community, business, investors and policymakers” (p. 7, Consultation paper).

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