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The Limits of Business Case Logic:
A case study of climate friendly banks

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ABSTRACT

This article examines whether and to what extent business case-induced voluntary corporate change can facilitate broader societal change. It does so through analysis of an empirical case study: banks and climate change. Specifically, it investigates whether it is prudent to put our faith in purely voluntary action as the mode by which banks assist timely transition to a low-carbon economy when such action is borne of business case logic. In so doing, this article provides practical insights into the limits of self-regulation, and contributes to the broader intellectual debate about self-regulation versus government intervention.

A. INTRODUCTION

In the past two decades, a variety of business strategists and environmental commentators have argued that the business community can successfully combine dual objectives of bottom-line growth and socio-environmental responsibility. This business strategy literature comprises a diverse range of theses such as eco-efficiency,[2] ecological modernization,[3] natural capitalism,[4] the triple bottom line,[5] stakeholder theory,[6] and beyond-compliance behavior to theorize and/or prove that 'going green' generates corporate financial benefit.[7] Benefits might be achieved by, for

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[2] Stephan Schmidheiny and Federico Zorraquin, *Financing Change: The Financial Community, Eco-Efficiency and Sustainable Development* (MIT Press, 1996).

[3] Andrew Gouldson and Joseph Murphy, *Regulatory Realities: The Implementation and Impact of Industrial Regulation* (Earthscan, 1998); John Dryzek, *The Politics of the Earth: Environmental Discourses* (Oxford University Press, 1997); Maarten A. Hajer, *The Politics of Environmental Discourse: Ecological Modernization and the Policy Process* (Clarendon Press, 1997).

[4] Paul Hawken, Amory B. Lovins and L. Hunter Lovins, *Natural Capitalism: The Next Industrial Revolution* (Earthscan, 1999).

[5] John Elkington, *Cannibals with Forks: The Triple Bottom Line of 21st Century Business* (Capstone Publishing, 1997).

[6] R. Edward Freeman**,** *Strategic Management: A Stakeholder Approach*. (Pitman, 1984); William M. Evan and R. Edward Freeman, 'A Stakeholder Theory of the Modern Corporation: Kantian Capitalism' in Tom L. Beauchamp and Norman L. Bowie (eds), *Ethical Theory and Business* (Prentice Hall, 1988) 75; Thomas Donaldson and Lee E. Preston, 'The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications' (1995) 20(1) *Academy of Management Review* 65.

[7] Michael E. Porter and Claas van der Linde, 'Green and Competitive: Ending the Stalemate' [1995] (September/October) *Harvard Business Review* 120; Michael E. Porter and Claas van der Linde, 'Toward a New Conception Of The Environment-Competitiveness Relationship' (1995) 9 *Journal of Economic Perspectives* 97; Ken Green, Peter Groenewegen and Peter S. Hofman (eds), *Ahead of the Curve: Cases of Innovation in Environmental Management* (Kluwer Academic Publishers, 2001).

example, preventing pollution and thereby cutting costs, gaining an increasing share of expanding 'green markets' or price premiums within them, more effective risk management and/or enhanced social reputation.[8] In other words, business can do well by doing good.[9]

Central to the business strategy literature is the concept of the business case. Referred to by some authors as 'the business case for sustainability' it can be described as a company "voluntarily doing something that improves not only its economic performance in absolute terms, but also its environmental and social performance"[10] whether or not environmental and social issues are caused through primary or secondary corporate activities.[11]

The purpose of this article is to extend thinking on the business case for sustainability. It will not add another voice to the debate about whether or when the 'green' business case can assist a company's bottom line. Instead, it examines the issue of whether and to what extent business case-induced voluntary corporate change can facilitate broader societal benefit. Specifically, it does so through analysis of an empirical case study of early-moving banks on climate change. In so doing, this article provides insight into practical issues of self-regulation borne of business case logic, and contributes to the broader intellectual debate about self-regulation versus government intervention.

Climate change is as much an economic issue as an environmental or ethical one. Global GHG emissions must peak no later than 2015 and then drop by one third by 2020 relative to business as usual if we are to stay within a 2°C guardrail of dangerous global warming.[12] The World Bank has estimated that this will require massive financial mobilization in the order of US$100-700 billion annually for research and development investments *alone* up from current financing of US$13 billion a year in public funds and $40-60 billion in private funding.[13] Similarly, trillions of dollars will be required to upgrade and expand the world's energy and transport infrastructure.[14] Accordingly, climate change mitigation will involve one of the largest global market and economic transitions in modern society.

Given this reality, more attention needs to be paid to the private finance sector's role in assisting emissions reductions and the transition to a low-carbon global economy. Specifically, private sector banks are global economic gatekeepers and financial intermediaries, which makes them a potentially critical actor in the transition to a low-carbon economy. This potential is summarized by Deutsche Bank:

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[8] Neil Gunningham, 'Shaping Corporate Environmental Performance: A Review' (2009) 19 *Environmental Policy and Governance* 215.
[9] Chris Laszio, *How the World's Companies Are Doing Well by Doing Good* (Greenleaf, 2008).
[10] Ulrich Steger (ed), *The Business of Sustainability: Building Industry Cases for Corporate Sustainability* (Palgrave MacMillan, 2004) 39.
[11] Oliver Salzmann, Aileen Ionescu-Somers and Ulrich Steger, 'The Business Case for Corporate Sustainability: Literature Review and Research Options' (2005) 23(1) *European Management Journal* 27.
[12] Bert Metz, 'The Climate Financing Problem: Funds needed for Global Climate Change Mitigation Vastly Exceed Funds Currently Available' in Richard B. Stewart, Benedict Kingsbury and Bryce Rudyk (eds), *Climate Finance* (New York University Press, 2009) 42; Deutsche Bank, *Deutsche Bank's Commitment to Addressing Climate Change* (Deutsche Bank, n.d.).
[13] World Bank, "Climate Smart' World Within Reach, says World Bank' (Press Release, 2010/068/DEC, 15 September 2009) <http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:22312494~pagePK:64257043~piPK:437376~theSitePK:4607,00.html>.
[14] World Bank, *World Development Report 2010: Development and Climate Change* (International Bank for Reconstruction and Development/World Bank, 2010).

> As *an asset manager* we can steer investments into low-carbon companies, as *a trader* we provide liquidity in the carbon market, and as *a capital markets participant* we can raise debt and equity capital to fund clean tech companies and projects and provide solutions to all clients who face the inevitable impact of climate change.[15]

Moreover, banks work with large corporate clients (both intensive greenhouse gas ('GHG') emitters and also clean tech innovators) and have a unique capacity to influence their own corporate network, which includes clients, suppliers and competitors.[16] As such, they are optimally placed to enroll other corporate actors in GHG mitigation efforts.

The net effect is that private sector banks are an important unit of study regarding the move to a low-carbon global economy. Through the banking industry's practices and its influence on other corporate actors, there is potential for large-scale change through client, supplier and competitor networks. That is, banks can set benchmarks not only for their own corporate governance climate strategies but also for their clients and suppliers, which then set such standards for their own clients and suppliers, and so on in an ever-widening web of corporate change.[17] In this way, 'enlightened' climate-related banking practices that are mainstreamed in the industry as a whole – and not just the praxis of early movers – could have potential to facilitate GHG emissions reductions through corporate networks. This unique and subtle potential of banks is termed the bank industry's 'network change potential' and it is for this reason that we need to consider how best to mobilize the banking industry as a whole.

Although Ceres has confirmed that "[b]anks have the reach, influence and access to capital required to lead the changes needed to expeditiously address global warming",[18] actions by early-movers are relatively recent and the industry as a whole is yet to follow suit. Early-moving banks are *voluntarily* adopting and outputting climate-related practices and products without legal compulsion: no international agreement is set to take the place of the Kyoto Protocol and national/regional climate change regulation is emerging and variable with some jurisdictions yet to legislate a carbon price or incentivize low-carbon technologies. Yet scholars and policy-makers have paid little attention to the banking industry's connection with climate change, including the levers and limits of its voluntary initiatives.[19]

This article explicitly builds on my previous empirical research, which investigated the drivers of climate-related bank initiatives.[20] That research evidenced that business case logic is the overarching driver. Specifically, the business case comprised profit increase (directly via fee generation and indirectly via competitive edge) and risk mitigation (financial, regulatory, and reputational). Crucial to these findings was a deeper understanding of 'corporate reputation' in business practice. The data showed that it comprises not only the well-established 'social reputation' but also a reputation for good business sense and delivering excellent service that helps large corporate clients to flourish, what I termed 'client service reputation'. For all

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[15] Deutsche Bank, *Deutsche Bank's Commitment to Addressing Climate Change* (Deutsche Bank, n.d.) 2.
[16] Megan Bowman, 'The Role of the Banking Industry in Facilitating Climate Change Mitigation and the Transition to a Low-Carbon Global Economy' (2010) 27 *Environmental and Planning Law Journal* 448.
[17] Ibid.
[18] Doug G. Cogan, *Corporate Governance and Climate Change: The Banking Sector* (Ceres, 2008) i.
[19] Doug G. Cogan, *Corporate Governance and Climate Change: The Banking Sector* (Ceres, 2008); Bettina Furrer, Marion Swoboda and Volcker Hoffman, *Banking & Climate Change: Stumbling into Momentum? An Analysis of Climate Strategies in More Than 100 Banks Worldwide* (SAM, 2009).
[20] Megan Bowman, 'Corporate Care and Climate Change: Implications for bank practice and government policy in the United States and Australia' (2013) 19(1) *Stanford Journal of Law, Business & Finance* (forthcoming).

interviewees, regardless of their jurisdiction or unit, client service reputation was a prime motivator for climate-related products, services and new market entry. In nearly all of the cases studied, large corporate and/or wealthy individual clients had approached a bank to seek solutions: not only for mitigating regulatory risk associated with extant or threatened carbon pricing, but even more so to capitalize on opportunities created by new markets. Banks are fighting for "a fixed universe of clients [and] a fixed size of the purse" (A2). So by helping corporate clients to survive and thrive in an increasingly carbon-constrained world, banks help themselves by enhancing their competitive advantage and thus fee generation. Under the impetus of client service reputation, banks could be agnostic about climate change; their 'green' driver was the greenback not a desire to save the world.

Moreover, interplay between reputation and regulatory context became apparent in that study by examining banks' perspectives of climate change as a risk or an opportunity. In large part, their perspective was jurisdiction-specific and shaped by regulatory context. The regulatory context included not only government interventions – namely a carbon price, financial incentives for renewables, a GHG reduction target, or even direct coercive social regulation such as the U.S. *Community Reinvestment Act of 1977* (12 U.S.C. 2901) ('CRA') – but also social pressure from non-government organization ('NGO') campaigns and civil society. The more sophisticated and stable the state interventions the more that banks saw climate change as an opportunity, and leveraged regulatory incentives to enhance their client service reputation, social reputation, and profits. The weaker or less certain the state interventions, then: (a) the more important NGO activity and voluntary industry standards became to mobilize better corporate behavior; and (b) the more likely that banks saw climate change as a risk. In such a regulatory context banks focused on strategies for downside prevention, particularly for protecting their social reputation.

In summary, the overarching driver for climate-related corporate changes by banks is business case logic and the underlying driving force is strong and simple: make money and do not lose money.

This article critically analyses the business case as driver. It seeks to address whether it is prudent to put our faith in purely voluntary standard-setting as the mode by which banks assist timely transition to a low-carbon economy, particularly when those benchmarks are borne of business case logic. In so doing it uses empirical data and analysis to examine how far and fast mainstreamed bank-created standards can take us down a low-carbon path.

The next Part describes the methodological approach to data collection and analysis for this research. Part 3 interweaves the business strategy literature on the business case with interview data from managers at early moving banks in market-based economies. It investigates inherent and economically rational limitations to business case logic; and considers whether and to what extent business case logic might facilitate only incremental change rather than the expeditious and transformational change required. Part 4 makes explicit the scholarly contribution of this research and considers future research regarding the implications of the findings for timely facilitation of climate change mitigation.

B. METHODOLOGY

I targeted early-moving banks due to their leadership and network change potential. The logic was to investigate the levers and limits of bank-instigated climate-related practices and to draw implications from those findings for optimal forms of climate finance regulation. 'Regulation' in this context is broadly conceived: it includes self-regulative industry measures as well as government interventions.

In summary, my sample comprised seven banks that were early-moving or 'leading' on the issue of climate change. I conducted 32 semi-structured interviews, comprising 19 interviews with internal (bank) respondents and 13 interviews with external (third-party) respondents. Interviews were conducted in the United States ('U.S.'), Australia, Europe and the United Kingdom ('UK') during May-June 2010 and September 2011.

I pinpointed early moving or 'leading' banks by cross-referencing the seven highest ranked banks in two ranking reports on climate change endeavors in the banking industry.[21] I then contacted the authors of those reports to confirm the rankings and clarify the leadership criteria used.[22] These banks were further confirmed as leaders in the space by multiple other sources, namely bank interviewees, NGOs, consultants, and mass media. Respondents and their organizations will not be identified in this article.

Bank respondents had intimate knowledge of the climate-related initiatives in each leading bank. Two to four people from different units within each leading bank were interviewed so as to ensure a variety of perspectives and responses for each case. The majority of interviewees were managers (titled 'managing director', 'executive director', 'director', 'vice president' or 'senior manager') who headed up units for renewable and clean technologies, equity and investment research, carbon trading, project and structured finance, and energy and power. I targeted this group of managers for their hands-on knowledge and implementation of climate-related practices, as well as their link to senior management and central policy within the bank. A minority of interviewees headed up corporate social responsibility ('CSR') and corporate sustainability units.

I also interviewed external respondents who could give additional perspectives on the role of banks in climate change mitigation generally and the leading banks' practices specifically. These respondents included: independent consultants on climate change to the finance sector and/or United Nations Environment Program Finance Initiative ('UNEPFI'); researchers who had authored reports on the topic; staff and the CEO of a niche climate change bank; the editor of a leading industry journal; and relevant members of NGOs and environmental activist groups.

C. THE LIMITS OF CORPORATE VOLUNTARISM: EMPIRICAL EVIDENCE AND FINDINGS

As stated in the Introduction, the overarching driver for climate-related corporate changes by banks is business case logic: make money and do not lose money. Importantly, the business case logic that drives banks is redolent in the business strategy field more generally. For example, in order to turn environmental strategy into competitive advantage, Reinhardt entreats companies to identify the fundamental business logic (in terms of risk management and value enhancement)

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[21] Doug G. Cogan, *Corporate Governance and Climate Change: The Banking Sector* (Ceres, 2008); Bettina Furrer, Marion Swoboda and Volcker Hoffman, *Banking & Climate Change: Stumbling into Momentum? An Analysis of Climate Strategies in More Than 100 Banks Worldwide* (SAM, 2009).

[22] Early moving or 'leading' banks fulfilled key criteria such as: climate corporate governance mechanisms (such as an environment charter, board oversight, and specific focus on 'climate change' as opposed to the more general 'environment'); risk management and project financing/lending practices that account for carbon intensity of clients and projects; climate-oriented corporate investment products (such as clean tech equities); high activity in carbon markets and funds; and high activity in advising/knowledge-sharing on climate change with clients, community, and governments.

peculiar to their company and context.[23] Similarly, Hoffman contends that the business case must drive corporate change and that companies need "a bottom line rationale or such efforts will be financially unsustainable".[24] To this end, Hawken, Lovins and Lovins contend that whether a business 'believes' in climate change or not is irrelevant; companies should adopt eco-efficient practices "simply because they make money".[25]

Yet, relying on business case logic as a modality of corporate change that can facilitate timely mitigation of global warming raises two key issues. The first issue is a logical one: business case logic has inherent and economically rational limitations. The second issue is organizational: business case logic can perpetuate business as usual ('BAU') and/or incremental change rather than expeditious and transformational change. These issues are explored in detail below.

1. Inherent Limitations to Business Case Logic

There are two main limitations to the business case as a driver for mainstreaming climate-related practices by banks. The first is that, by definition, if an initiative is not profitable or the costs outweigh the benefits - that is, if there is *not* a business case to do it - then banks will not make the change. The second important limitation is that, at present, there exists a competing business case to support GHG-intensive clients and projects. Both limitations are seen in action when examining the size of the current renewables market.

The Requirement of a Business Case for Green Uptake

The first limitation – the prerequisite of a business case for green uptake - is exemplified by Bank A. This bank appeared to be the most climate change conscious and proactive leading bank in my sample. It had a passionate Chair who provided leadership on green issues and supported climate-related business initiatives; some of its managers and advisers had green credentials and were brought onboard to progress the bank's low-carbon agenda; other managers held strong personal beliefs about environmental stewardship and were proactive in initiating green services. This bank demonstrated innovation around climate services and products and climate change had been elevated to the corporate governance level under senior management oversight. Finally, the bank was the only one in my sample to sign onto all three voluntary Principles in this space, being the Equator Principles, the Carbon Principles, and the Climate Principles. Despite all of this, it was clear from interviewees that if a 'green' initiative did not make good business sense then it would not get traction.

For example, interviewees at Bank A stated that there had to be "revenue streams associated with climate change" and that green initiatives needed "a sound business case and to create value for shareholders" (A1). They stated that a climate-related unit needed to be commercially viable in order to get started: "If it wasn't then we simply couldn't do it, we wouldn't get the management funding and support" (A2). And whilst the Board had shown willingness to back new and risky climate-related initiatives, those initiatives needed to become self-sustaining in order to persist. For example: "The success of this [climate research unit] is gauged by external and internal feedback and how much money it makes. We have passed the honeymoon period so it must be financially sustainable now or it wouldn't exist" (A3).

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[23] Forest Reinhardt, *Down to Earth: Applying Business Principles to Environmental Management* (Harvard University Press, 2000).
[24] Andrew. J. Hoffman, 'Climate Change Strategy: The Business Logic Behind Voluntary Greenhouse Gas Reductions' (2005) 47(3) *California Management Review* 21, 23.
[25] Hawken, B. Lovins and Lovins, above n 4, 243.

An interviewee from a different bank summarized it thus: "We are massive creators of shareholder wealth and massive contributors to the economy" (G1) and therefore, as stated by yet another interviewee, "No-one is expecting banks to be charities…[or] to finance a bunch of unprofitable projects" (E1). Put simply: "we recognize we are a bank and we need to make money" (E1).

The problem with building a business case for climate-related initiatives is that profit momentum from gaining new large clients may take time to materialize; and some initiatives will have only indirect consequences on the bottom line, such as enhancing a company's social reputation or its capacity to attract and retain talented staff.[26] Thus, the 'materiality' of the business case may deter voluntary corporate environmental uptake.

This limitation is acknowledged in corporate sustainability literature, which highlights how the business case can be difficult to detect and/or marginal in practice given that "the economic value of more sustainable business strategies…only materializes in the long term".[27] The problem is that, as noted by Dermine, we live in "a world in which financial markets reward short-term reported profits".[28] As such, the focus on short-term profit can trump long-term value and be a significant barrier to corporate environmental change. Generally, if public companies and especially financial firms, "cannot demonstrate tangible economic success in the here and now [then] there may be no long term to look forward to".[29]

Data in this study reflect these concerns. An initiative will not get Board support unless proponent-managers can show a clear and immediate business case. Arguably this is so for all new initiatives. Yet for 'green' initiatives in particular the short-termism limitations identified in the literature were apparent in the data, namely: (a) disjunction between seeing how environmental-social risks and opportunities translate into fiscal ones, especially given that sustainability-related gains or losses can be difficult to quantify, and/or (b) a lag between green implementation and financial results. Either of these limitations in business case logic has potential to impede *en masse* bank activity in climate-related spaces outside of long-term pension fund investment.

The Countervailing Business Case for Non-Green Initiatives

The second key limitation of the business case as the driver for mainstreaming climate-friendly bank practices is that, at present, there still exists a countervailing business case to support GHG-polluting clients and projects.[30] Banks will continue to work with these clients, which often have relationships with a number of different departments within the same bank and are therefore a lucrative overall source of fee generation. Retaining such large clients is inextricably entwined with the highly competitive nature of the banking industry. Ostracizing such clients is equivalent to handing them on a silver platter to a competitor and missing out on a part of 'the purse'. It also ties back to client service reputation via client satisfaction: "For any bank a huge percentage of business is mining companies. We can't afford to turn business away and we wouldn't be looking after our clients if we did" (E1).

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[26] Clarissa Lins et al, 'Corporate Sustainability in the Brazilian Banking Sector' (Research Paper No IMD 2008-07, IMD International, 2008).
[27] Salzmann, Ionescu-Somers and Steger, above n 11, 33.
[28] Jean Dermine, 'Bank Corporate Governance, Beyond the Global Banking Crisis' (Working Paper No 2011/33/FIN, INSEAD, 14 March 2011) 9.
[29] Gunningham, above n 8, 218.
[30] Richardson (2008) also acknowledges this limitation in relation to institutional investors and socially responsible investment.

Australian banks provide a good illustration of this point. Interviewees described how, in recent years, they have become very focused on 'relationships' with clients and how being trusted as a good business adviser is central to that dynamic. In addition, Australia is a coal-rich jurisdiction, it has only four big banks, and coal clients comprise a major part of their energy/power portfolios. Making any radical voluntary changes against their coal clients is tantamount to compromising client service reputation and therefore compromising financial returns. Banks need to balance competing client interests with their own financial and reputational interests. Coal is a short- to mid-term reality; low carbon energy sources are a mid- to long-term proposition. Australian banks are willing to hedge their bets by taking on renewable energy clients, but they are not willing to drop lucrative coal clients of their own volition. For example:

> We did two [renewable] transactions that created positive feedback from the market, which led to more renewable energy business that in turn lifted our reputation in that space. That's important for the future. But reputation with the coal-fired sector is also important to us, especially regarding re-financing, which is happening now (F2).

Nonetheless, business case logic comprises risk mitigation, which drives incremental change. This was evident in two categories of climate-related bank initiatives. First, all leading banks had adopted enhanced due diligence processes, as part of the Carbon or Equator Principles, or through heightened internal risk management procedures. Several interviewees described enhanced due diligence as an indirect deterrence for clients to continue in heavy polluting activities due to the extra hoops involved in seeking finance. Second, some banks had become "strategic advisers to migrate fossil fuel clients across" to a lower-carbon existence (C2) which included modernizing or decommissioning old coal plants on the one hand and financing environmental technology for plants and renewables on the other. In other words, instead of dropping clients entirely, banks will influence clients "to change their ways" (E1).

It is here that we get an even deeper understanding of the interplay between client service reputation and the business case. Banks will not drop clients without extremely serious cause. As one interviewee stated:

> We are a well-regarded energy bank, so energy clients – whether coal, gas or renewable - come to us for business…We are not going to pick sides in an emotive turf war. We need to be a trusted adviser (G4).

It becomes clear that client service reputation is a double-edged sword in terms of voluntary corporate action. On the one hand it mobilizes banks to innovate new products and to become active in green spaces due to the desire for competitive advantage and enhanced fee generation. Yet, concomitantly and ironically, client service reputation impedes far-reaching entrepreneurialism. Even leading banks are not willing to voluntarily make radical business changes lest they compromise their competitive edge and financial returns. They will not irrationally sacrifice lucrative clients on the 'green' altar. So, while client service reputation is a strong motivator for banks to voluntarily drive action in a 'greener' direction, it is a simultaneous brake on driving too far down that path.

Current Market Limitations

The above logical limitations to the business case are brought clearly into focus when we observe the current size of renewable energy and clean tech markets.

Banks and their clients are actively looking for opportunities associated with climate change as much as they are trying to mitigate risks. As such, the 'opportunity' component of the business case is an increasingly important motivator for corporate green uptake. Renewable energy and clean tech spaces present such opportunities for banks. These industries are lucrative – over $1 trillion of private investment went into renewable energy and clean tech for the period 2007–2010 – and they have long-term potential for significant investment opportunities.[31] For these reasons, most interviewees stated that being in the renewables space is core to their bank's business, with one interviewee describing it as "pretty mainstream now in the [bank] industry generally" (B1).

However, renewable energy and clean tech markets are considerably smaller in size than traditional energy markets; they are regarded as nascent and may not reach maturation for decades. This has obvious repercussions for bank activity in both low-carbon and fossil fuel spaces. As stated by one interviewee:

> We're currently doing doubles and singles not multiples and home runs [in the renewables space] because although the market is currently $100 billion in size that is still not a huge market for a big investment bank (C3).

The comparatively small size of alternative energy markets ensures that banks will not make radical changes that have a chilling effect on fossil fuel clients. There is no logical reason for doing so if there is no guaranteed and sizeable return to warrant or entice such a switch. In other words, it would not make good business sense. Neuhoff et al. found that climate finance was stifled for this very reason:

> With the current regulatory framework unable to sufficiently incentivize low-carbon project developers and thereby stimulate a strong low-carbon project pipeline, investors do not have enough projects, or sufficiently large projects, to which they can easily provide finance. Consequently, they are unable to realize the necessary economies of scale.[32]

The bank industry is driven by profit and client service; the current size of the renewables market is not conducive to banks' ostracizing, let alone excising, fossil fuel clients and funding only alternative energy initiatives. Thus we have a current dilemma whereby the renewables market is not yet significant enough to drive radical changes to bank practices, yet private finance is required to help bring low-carbon energy solutions to scale. I will return to this conundrum in Part 4.

2. Going the Distance: Standard-Setting and Real Change

The second issue is whether purely voluntary corporate action borne of business case logic can take us far or fast enough down a low-carbon path.

To address this issue we must ask 'what is being embedded as the industry norm?' The concern is that a low industry benchmark will not be sufficient to create core or substantive change to corporate practices. Specifically, voluntary changes driven by business case imperatives may result in low standard-setting if such changes target only easily-achieved cost efficiencies or 'low hanging fruit' (e.g. through risk management and cost reductions). Certainly, authors such as

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[31] Ethical Markets, *Green Transition Scoreboard* (30 July 2010) <http://www.greentransitionscoreboard.com/>.

[32] Karsten Neuhoff et al, *Structuring International Financial Support to Support Domestic Climate Change Mitigation in Developing Countries* (Climate Strategies, 2009) 7.

Steger and also Hoffman,[33] who advocate the business case as driver for corporate greening, highlight how 'easy wins' can be achieved through increased operational- or energy-efficiency measures rather than introducing environmental programs. Indeed, Salzmann, Ionescu-Somers and Steger suggest that this is the basis of the environmental dimension of the business case.[34]

'Efficiency' arguments are an attractive and pragmatic selling point for corporate environmental change; they go to the heart of win-win discourse. For example, energy efficiency is germane to theories of natural capitalism and eco-efficiency because it can, apparently, radically reduce GHG emissions without radically altering BAU or financial output.[35] In this way however, efficiency arguments advocate the 'no-brainers' of good management rather than the harder work of corporate sustainability.[36] As noted by Bebbington,[37] efficiency on its own is a necessary but insufficient condition for sustainability. Spence further explains that "efficiency gains can potentially be undone by business growth" with the outcome that a business may create a larger overall environmental footprint despite making per unit eco-efficiency improvements.[38]

The concern is that 'no brainers' can result in minimalist change being embedded as the industry norm, with the result that doing more than the minimum is anathema. Importantly, low industry standards tend to comprise BAU with peripheral changes only. The literature on this issue, particularly in critical management studies and social-environmental accounting, contends that when this happens, businesses are not 'doing' sustainability so much as BAU.[39] The result is that the magnitude of environmental issues and the level of corporate change required to address them is masked or deflected.

Some scholars have termed this phenomenon as corporate or managerial 'capture' of the CSR agenda.[40] In short, this comprises "a perceived necessity or desire to capture and control conceptions of CSR within conventional business norms",[41] that is, within the parameters of BAU. Other scholars label it the 'middle' or 'third' way.[42] This term identifies a pragmatic

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33 Ulrich Steger (ed), *The Business of Sustainability: Building Industry Cases for Corporate Sustainability* (Palgrave MacMillan, 2004); Andrew. J. Hoffman, 'Climate Change Strategy: The Business Logic Behind Voluntary Greenhouse Gas Reductions' (2005) 47(3) *California Management Review* 21.

34 Salzmann, Ionescu-Somers and Steger, above n 11.

35 Robert U. Ayres and Edward Ayres, *Crossing the Energy Divide: Moving from Fossil Fuel Dependence to a Clean-Energy Future* (Prentice Hall, 2010).

36 Salzmann, Ionescu-Somers and Steger, above n 11.

37 Jan Bebbington, 'Sustainable Development: A Review of the International Development, Business and Accounting Literature' (2001) 25(2) *Accounting Forum* 128.

38 Crawford Spence, 'Social and Environmental Reporting and Hegemonic Discourse' (2007) 20(6) *Accounting, Auditing & Accountability Journal* 855, 870.

39 Markus J. Milne, Helen Tregidga and Sara Walton, 'Words not actions! The Ideological Role Of Sustainable Development Reporting' (2009) 22(8) *Accounting, Auditing & Accountability Journal* 1211.

40 See, eg, Brendan O'Dwyer, 'Conceptions of Corporate Social Responsibility: The Nature of Managerial Capture' (2003) 16(4) *Accounting, Auditing & Accountability Journal* 523; Rob H. Gray, Reza Kouhy and Simon Lavers, 'Corporate Social and Environmental Reporting: A Review of the Literature and a Longitudinal Study of UK Disclosure' (1995) 8(2) *Accounting, Auditing & Accountability Journal* 47; Crawford Spence, 'Social and Environmental Reporting and Hegemonic Discourse' (2007) 20(6) *Accounting, Auditing & Accountability Journal* 855.

41 Brendan O'Dwyer, 'Conceptions of Corporate Social Responsibility: The Nature of Managerial Capture' (2003) 16(4) *Accounting, Auditing & Accountability Journal* 523, 532.

42 Markus J. Milne, Helen Tregidga and Sara Walton, 'Words not actions! The Ideological Role Of Sustainable Development Reporting' (2009) 22(8) *Accounting, Auditing & Accountability Journal* 1211; Pushkala Prasad and Michael Elmes, 'In the Name of the Practical: Unearthing the Hegemony of Pragmatics in the Discourse of Environmental Management' (2005) 42(4) *Journal of Management Studies* 845;

approach by business to green issues that sits between "free-market fundamentalism" on one hand and "the green left" on the other hand.[43] However, these scholars argue that the demands of the environment and development are conflicting; and business discourse that simplifies the conflict prevents far-reaching environmental-corporate change.[44]

Importantly, there are two outcomes when corporate capture/ middle way framing creates or perpetuates the impression that meaningful change is occurring when it is not. First, it creates a missed opportunity to facilitate real solutions to pressing problems. In other words, it "crowds out and closes down alternative… principles and practices that might actually be better for conserving the Earth".[45] Second, it can result in legitimation of the status quo and thus *resistance* to required change by keeping BAU and just adding 'a lemon twist'.[46]

In this sense, it is arguable that voluntary 'green' corporate changes motivated by business case logic are not so much a bridge to salvation as a tweak to the status quo. In the context of climate change, Vogel provides useful illustration of this conundrum.[47] Vogel uses BP to exemplify how some climate-related gains are peripheral when compared to core business activities; and that responsible behavior is limited when the business case for green uptake relies on market demand and consumer patronage. BP had invested over $200 million in solar power between 1995-2001, yet in 2001 alone it had spent $8.5 billion to explore and produce fossil fuels.[48] Putting that in perspective, for the year 2002 BP's investment in solar equaled less than 0.5% of its expenditure on petroleum development and only 0.02% of its entire net worth.[49] Moreover, even though BP had reduced its own GHG emissions and created a new market for its natural gas waste, the significance of BP's contribution to the production of GHG emissions is not through its own pollution. Rather, Vogel notes that it is "primarily from the consumption of the fossil fuels it markets and whose sales continue to form the basis of its business".[50] In other words, at its core, the business of BP is to explore and produce oil and to disseminate that oil to the world. Tweaking the edges of that core business, whilst laudable, does not create significant change to the status quo.

Tony Tinker, Marilyn Neimark and Cheryl Lehman, 'Falling Down the Hole in the Middle of the Road: Political Quietism in Corporate Social Reporting' (1991) 4(2) *Accounting, Auditing & Accountability Journal* 28.

[43] Milne, Tregidga and Walton, above n 39, 1236.

[44] Crawford Spence, 'Social and Environmental Reporting and Hegemonic Discourse' (2007) 20(6) *Accounting, Auditing & Accountability Journal* 855; Rob H. Gray and Jan Bebbington, 'Environmental Accounting, Managerialism and Sustainability: is the Planet Safe in the Hands of Business?' (2000) 1 *Advances in Environmental Accounting and Management* 1.

[45] Milne, Tregidga and Walton, above n 39, 1239.

[46] Brendan O'Dwyer, 'Conceptions of Corporate Social Responsibility: The Nature of Managerial Capture' (2003) 16(4) *Accounting, Auditing & Accountability Journal* 523; Markus J. Milne, Helen Tregidga and Sara Walton, 'Words not actions! The Ideological Role Of Sustainable Development Reporting' (2009) 22(8) *Accounting, Auditing & Accountability Journal* 1211; Crawford Spence, 'Social and Environmental Reporting and Hegemonic Discourse' (2007) 20(6) *Accounting, Auditing & Accountability Journal* 855; Tony Tinker, Marilyn Neimark and Cheryl Lehman, 'Falling Down the Hole in the Middle of the Road: Political Quietism in Corporate Social Reporting' (1991) 4(2) *Accounting, Auditing & Accountability Journal* 28.

[47] David Vogel, *The Market for Virtue: The Potential and Limits of Corporate Social Responsibility* (Brookings Institution Press, 2005).

[48] Cait Murphy, 'Is BP Beyond Petroleum? Hardly' [2002] (September) *Fortune* 44.

[49] Paul Driessen, *Eco-Imperialism* (Free Enterprise Press, 2003).

[50] Vogel, above n 47, 127.

These concerns about the core or substantive nature of voluntary corporate change have clear resonance in the context of climate-related business changes by banks. Lundgren and Catasús note that:

> It appears that banks have taken a number of steps, which, taken together, emphasize a responsibility towards the natural environment. The level of ambition can, however be questioned. What would the critical stakeholder with…knowledge of scientific facts…think about the steps that have been taken?[51]

To this end, NGOs and some academics have questioned the ingenuity of leading banks' commitment to a 'core' green agenda via a number of criticisms. For example: that 'new' practices such as carbon trading and climate risk due diligence fall within the scope of current practice and are therefore simply logical as opposed to truly 'green' (NGO-D1, NGO-A1; BankTrack 2010);[52] that voluntary Principles are sub-optimal for achieving environmental and sustainability objectives;[53] and, perhaps the most vocal criticism, that funding for fossil fuel projects continues at disproportionate levels to that for renewables and clean tech.[54]

My empirical data reveal that there are some genuine innovations initiated voluntarily by leading banks that have potential to facilitate corporate GHG reductions through client networks in a ripple-out effect as postulated in the Introduction. Examples include Bank C's outright veto on lending to companies that practice mountain top removal coal mining and Bank A's climate change indices that fundamentally change how fund managers classify and allocate institutional investments: "The classification determines the asset allocation process. Fund managers have no translator between the way they see the world and the way the world is changing. We offer them a different view" (A2).

However, the data also evidence grounds for concern regarding the core and substantive nature of voluntary climate-related changes by leading banks, as detailed below.

'Green' activities as BAU?

The evidence shows that banks are largely capitalizing on what they already do well. For example, interviewees involved in carbon trading noted that it was another asset class to be exploited:

> [The bank] is active in carbon trading in the same way it is active in other trading areas such as oil, gas, electricity and coal trading desks. Therefore the carbon market is a natural addition to these desks. It makes no sense to trade in other commodities and not carbon (E2).

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[51] Maths Lundgren and Bino Catasús, 'The Banks' Impact On the Natural Environment - On the Space Between 'What Is' and 'What If'' (2009) 9 *Business Strategy and the Environment* 186, 186.

[52] BankTrack, *Bold Steps Forward: Towards Equator Principles that Deliver to People and the Planet* (BankTrack, 2010).

[53] BankTrack, *Meek Principles for a Tough Climate: Why the Carbon and Climate Principles Will Not Stop the Melting of the Ice* (BankTrack, 2009); RAN (Rainforest Action Network), *The Principle Matter: Banks, Climate & the Carbon Principles* (RAN, 2011); Richard Macve and Xiaoli Chen, 'The 'Equator Principles': A Success for Voluntary Codes?' (2010) 23(7) *Accounting, Auditing & Accountability Journal* 890; Niamb O'Sullivan and Brendan O'Dwyer, 'Stakeholder Perspectives on a Financial Sector Legitimation Process: the Case of NGOs and the Equator Principles' (2009) 22(4) *Accounting, Auditing & Accountability Journal* 553.

[54] Heffa Schücking et al, *Bankrolling Climate Change* (Urgewald, 2011); RAN (Rainforest Action Network), *Banks, Climate Change & the New Coal Rush* (RAN); Greenpeace, *Pillars of Pollution: How Australia's Big Four Banks Are Propping Up Pollution* (Greenpeace, 2010); BankTrack, *Big Banks Warned to Steer Clear of Coal India Share Offer* (BankTrack, 2013).

For some banks this is also true of signing onto voluntary Principles:

> In my own view I don't really think [the Carbon Principles] impact upon the way we do business because we are already practicing a lot of what is presented in them regarding risk assessment and diligence levels. It wasn't a lot of effort to sign up and agree to all those things (B2).

It is important that banks capitalize on their financial intermediation role to facilitate climate change mitigation: this is their unique gift to helping solve the climate crisis. However, these data evidence that the 'greening' of some bank activities are well within BAU. For this reason, NGOs claim that banks "do not get green bragging rights" (NGO-D1) for these particular activities.[55]

Certainly, the act of corporations signing onto voluntary industry codes has drawn general criticism for providing symbolic appearance of action without delivering substantive environmental and social outcomes.[56] Regarding banks, most attention has been directed at the Equator Principles, which have been in force the longest: they were launched in 2003, revised in 2006 and again in 2013, coming into force as EP III on June 4 2013.[57] Criticisms of this voluntary code have focused mainly on two perceived shortcomings: limited coverage; and a lack of accountability mechanisms. In relation to limited coverage, the Equator Principles apply only to project finance activities above $10 million (as of 2006) and NGOs argue that this covers only "a small percentage of the environmental and social impacts of the financial sector as a whole".[58] Indeed, two NGO respondents (NGO-A1, NGO-D1) pointed out in interview that corporate finance activities comprise a much larger part of bank balance sheets than project finance. As such, some commentators posit that regulating project finance represents low-hanging fruit for financial institutions and deflects attention from "other fundamental areas of concern" in banking practice.[59] In relation to accountability, NGOs and legitimacy scholars have criticized the absence of clear accountability mechanisms in the Equator Principles at organizational or project levels, arguing that there is little opportunity to evaluate environmental results 'on the ground' or assess whether "the essential machinery" of a bank has changed or improved.[60]

In contrast, several authors in recent years have argued that assessing 'effectiveness' of voluntary codes may encompass more than just measuring outcomes by facilitating organizational learning and dissemination of best practices among adopting and non-adopting firms alike.[61] Specifically,

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[55] See also, BankTrack, *Bold Steps Forward: Towards Equator Principles that Deliver to People and the Planet* (BankTrack, 2010); BankTrack, *Big Banks Warned to Steer Clear of Coal India Share Offer* (BankTrack, 2013).
[56] Niamb O'Sullivan and Brendan O'Dwyer, 'Stakeholder Perspectives on a Financial Sector Legitimation Process: the Case of NGOs and the Equator Principles' (2009) 22(4) *Accounting, Auditing & Accountability Journal* 553; Blake E. Ashforth and Barrie W. Gibbs, 'The Double-Edge of Organizational Legitimation' (1990) 1(2) *Organizational Science* 177; Michael J. Lenox and Jennifer Nash, 'Industry Self-Regulation and Adverse Selection: A Comparison Across Four Trade Association Programs' (2003) 12(6) *Business Strategy and the Environment* 343; Pratima Bansal and Trevor Hunter, 'Strategic Explanations for the Early Adoption of ISO 14001' (2003) 46 *Journal of Business Ethics* 289.
[57] Equator Principles, *Equator Principles III* <http://www.equator-principles.com/index.php/ep3/ep3>.
[58] Niamb O'Sullivan and Brendan O'Dwyer, 'Stakeholder Perspectives on a Financial Sector Legitimation Process: the Case of NGOs and the Equator Principles' (2009) 22(4) *Accounting, Auditing & Accountability Journal* 553, 566.
[59] Ibid 555.
[60] Blake E. Ashforth and Barrie W. Gibbs, 'The Double-Edge of Organizational Legitimation' (1990) 1(2) *Organizational Science* 177, 181.
[61] Thomas P. Lyon and John W. Maxwell, 'Environmental Public Voluntary Programs Reconsidered' (2007) 35(4) *Policy Studies Journal* 723; Nicole Darnall and Stephen Sides, 'Assessing the Performance of Voluntary Environmental Programs: Does Certification Matter? (2008) 36(1) *Policy Studies Journal* 95.

some scholars have suggested that the very act of adopting the Equator Principles "may be both evidence of and a catalyst for cultural change"[62] within not only adopting banks but also lending syndicates.[63]

It was not the aim of this study to investigate the effectiveness of voluntary Principles in delivering improved environmental outcomes, or whether banks are strictly complying with them. Arguably, however, the main aim of the Equator Principles and the Carbon Principles is mitigation of financial, regulatory and (social) reputational risks. There is no doubt that risk mitigation, as a crucial component of the business case, is an important first step in corporate change and a strong driver for some banks to go green(er). Nonetheless, it is a first step only. The data show that when motivated by opportunity enhancement, banks become proactive and innovative in order to get a bigger slice of the pie (e.g. Bank A's investment indices). Opportunities can present a break with usual practice or can motivate the bank to leap two steps ahead of the curve instead of just one logical step further down the BAU path. Conversely, banks that are primarily driven by risk mitigation are reactive; their aim is to keep BAU running as smoothly as possible. And, as Bansal and Roth found,[64] when a firm's goal is to minimize risks and costs then it will aim only to meet standards and not exceed them (satisfice).[65]

Satisfice was clearly evident in the Australian data. Most Australian interviewees revealed that there had been little change to BAU in the past five years, with the exception of enhanced due diligence processes for climate risks. They further noted that corporate clients were similarly reactive, stating that "you'd be hard pressed to find a top 100 ASX company that has its head around the carbon issue" (G1) and that clients were "in no mood to make $100 million investment decisions in a climate of uncertainty" (G2). It is only since the advent of a carbon price that Australian banks and their clients are going beyond adoption of voluntary codes to seek opportunities. In contrast, leading banks in Europe (where climate regulation is well-established) and even in the U.S. (where federal incentives and a threatened carbon price existed at the time of interviews) are motivated by opportunities more so than risk mitigation. In these jurisdictions, leading banks have developed more innovative financial solutions around climate change mitigation.

Funding Practices and Client Service Reputation

Another concern regarding the core and substantive nature of climate-related changes by leading banks is the nature of their financing activities. NGOs around the world have highlighted a disparity between coal- and green-funding by banks. Coal-fired plants account for nearly one half

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[62] John M. Conley and Cynthia A. Williams, 'Global Banks as Global Sustainability Regulators?: The Equator Principles' (2011) 33(4) *Law & Policy* 542, 546.

[63] Deborah E. Rupp, Cynthia A. Williams and Ruth V. Aguilera, 'Increasing Corporate Social Responsibility through Stakeholder Value Internalization (and the Catalyzing Effect of New Governance): An Application of Organizational Justice, Self-Determination and Social Influence Theories' in Marshall Schminke (ed), *Managerial Ethics: Managing the Psychology of Morality* (Routledge, 2010) 69; Heiko Spitzeck, 'Organizational Moral Learning: What, If Anything, Do Corporations Learn from NGO Critique?' (2009) 88 *Journal of Business Ethics* 157.

[64] Pratima Bansal and Kendall Roth, 'Why Companies Go Green**:** A Model of Ecological Responsiveness' (2000) 43(4) *Academy of Management Journal* 717.

[65] Of course, risk mitigation may produce innovation in circumstances where the actual survival of the business is threatened by a crisis situation. E.g. Dillard et al. (2004) note that fundamental shifts in market composition and competitive characteristics forced the U.S. coal, textile and railroad industries to reconceptualize organizational and technical processes. However this was not evidenced by the data in this study.

of man-made CO_2 emissions.[66] As such, NGOs argue that funding renewable and clean tech projects while continuing to fund fossil fuel projects is counterproductive to the aim of a low-carbon economy. For example, the Rainforest Action Network (RAN) has described banks that fund coal as:

> the ATMs for a dirty industry that is bad for health and bad for business. Coal is the ultimate subprime investment for the climate. We cannot solve climate change if banks continue to prop up this risky and outdated industry.[67]

For these reasons, a European NGO respondent explained how his organization had commenced a project that endeavors to assess the carbon implications of a bank's lending and investment activities using the 2°C guardrail as a benchmark. Traditionally, banks have been benchmarked against each other. However this NGO respondent contended that a comparative yardstick was not appropriate or sufficient in the context of climate change mitigation:

> Right now there is nowhere near a consistent approach by banks. It's like saying you're 15% pregnant: either you're doing climate change mitigation or you're not. They need to be saying '2°C is a challenge for us and we will tackle it' (NGO-A1).

Furthermore, NGOs argue that amounts of funding for fossil fuel projects far outweigh those for low-carbon initiatives, making the green efforts of banks tantamount to greenwash. For example, RAN alleged that Citi's commitment in 2007 of US$50 billion over 10 years to address global warming amounted "to less than 0.2 percent of the company's $2.2 trillion in assets".[68] The report continues: "What is Citi doing with the other 99.8 percent? In 2006 Citi financed 200 times more money for dirty energy than it did for alternative energy".[69] Similar claims have been leveled at the big four Australian banks with Profundo evaluating that Australia's big banks have invested over AU$5 billion into coal (mining, burning, transporting) and only AU$0.78 billion into renewable energy.[70] Greenpeace has asserted that "[m]ajor banks such as ANZ and Westpac have happily accepted sustainability awards while continuing to invest hundreds of millions of dollars into polluting coal stations".[71] Such allegations echo Vogel's critical analysis of BP above.

Interestingly, interviewees highlighted a decline in finance for new coal in the U.S. and Australia since 2007, citing the reasons as a mix of tougher EPA approvals, increased NGO pressure, and the prospect of a carbon price. Nonetheless, my data show that leading banks in jurisdictions that (a) are rich in fossil fuels and/or (b) do not have well-established climate-related federal regulation in place - such as the U.S. and Australia - are cautious in sending signals that could be interpreted as 'choosing' renewable energy client interests over more lucrative fossil fuel ones. In these jurisdictions, coal and oil entities comprise a key component of banks' client bases. For reasons of competitiveness and client service reputation, banks will not readily drop these clients. As stated by one U.S. interviewee: "we don't walk away from long-standing clients easily if an activity is not illegal" (D1). An Australian interviewee gave a more textured response:

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[66] U.S. EPA (Environmental Protection Agency), *Clean Energy: Air Emissions* (25 September 2013) <http://www.epa.gov/cleanenergy/energy-and-you/affect/air-emissions.html>.

[67] Enews Park Forest, 'US Banks Risk Public Health and Climate by Financing Coal', *ENews Park Forest* (online), 1 May 2012 <http://www.enewspf.com/opinion/analysis/33080-us-banks-risk-public-health-and-climate-by-financing-coal-.html>.

[68] RAN (Rainforest Action Network), *Banks, Climate Change & the New Coal Rush* (RAN) 5.

[69] Ibid.

[70] Profundo Economic Research, 'Australian Banks Financing Coal and Renewable Energy: A Research Paper Prepared For Greenpeace Australia' (Research Paper, Profundo).

[71] Greenpeace, *Pillars of Pollution: How Australia's Big Four Banks Are Propping Up Pollution* (Greenpeace, 2010) 3; See also, BankTrack, *Big Banks Warned to Steer Clear of Coal India Share Offer* (BankTrack, 2013).

> Because our clients are mixed [between fossil fuel and low-carbon], it's always dangerous to go too strong one way or the other. We are inherently conflicted due to our client mix. Banks usually don't like to advocate on any issue for that precise reason: they don't want to piss off clients (F2).

For similar reasons, interviewees showed distaste for initiating preferential loans that have the effect of rewarding low-carbon clients and penalizing GHG-intensive ones. This empirical reality is in stark contrast to theoretical commentary that banks can and ought to charge differentiated interest rates depending on the green performance of the borrower (NGO-D1).[72] For example, Jeucken writes that an inherent activity of banks is pricing risk; therefore interest rate differentiation based on 'sustainability' (or lower environmental risks) is justified from a risk perspective.[73] An important by-product is that banks "support the good-doers and offset the wrongdoers"[74] and thus "contribute to sustainable entrepreneurship" through their financing policies.[75]

In contrast, my data show that preferential lending is unlikely to occur of banks' own volition. No interviewee supported it. Two interviewees at the same bank commented that their bank was acting sufficiently by virtue of having a renewables team and a sustainability department. Another interviewee at a different bank responded that lending conditions are decided on a case-by-case basis using risk metrics and good business sense, not by imposing ethical 'values'. He stated that:

> Sustainability is a strategic game. You achieve it through portfolio limits and pricing risk…If a coal station is giving us lots of business in Asia then we'll do the deal; and we might decline a renewable project because the client owns a leaking nuclear plant overseas (G1).

Two other interviewees made clear that preferential lending to incentivize clean energy activity is "not part of what we do on a daily basis" (C3) and too far outside BAU to be considered seriously. For example:

> The general philosophy of the bank is that we facilitate and give equal service to all clients. Giving preferential rates to renewable energy creates a difficult situation regarding why the bank is making certain choices. We need an economic rationale for doing this. It's not a bank's role to fudge the system. Get entrepreneurs or governments to incentivize (B1).

Consistent with 'BAU with a lemon twist', I found that leading banks are willing to engage in enhanced due diligence processes instead of preferential lending because it is a logical step for banks to extend their current due diligence practices to include 'climate risk'. Indeed, doing so is consistent with their established processes for evaluating environmental, social and governance (ESG) and financial risks associated with any new client or project. Importantly, enhanced due diligence does not involve any perceived ethical or value judgment:

> We don't bar sectors on the basis of legitimacy. It's a risk management process… We price risks associated with different industries…not because of some moral judgment (F2).

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[72] Marcel Jeucken, *Sustainability in Finance: Banking on the Planet* (Eburon Delft, 2004); Clarissa Lins et al, *Corporate Sustainability in the Brazilian Banking Sector* (*IMD 2008-07)* (IMD International, 2008).
[73] Marcel Jeucken, *Sustainable Finance and Banking: The Financial Sector and the Future of the Planet* (Earthscan, 2001); Marcel Jeucken, *Sustainability in Finance: Banking on the Planet* (Eburon Delft, 2004).
[74] Lundgren and Catasúsm, above n 51, 190.
[75] Marcel Jeucken, *Sustainability in Finance: Banking on the Planet* (Eburon Delft, 2004) 2.

Nonetheless, several interviewees opined that enhanced due diligence is an indirect deterrent for high-polluting activities and a mechanism through which banks can subtly "influence changes in economic activity" (B2).

So, at first glance, my data on preferential lending are similar to those of Lundgren and Catasús who found that the standard answer from credit managers in Swedish banks was "it is not our role to promote certain [environmental] values in the lending process".[76] For leading banks, taking an "economic not emotional" (B1) approach to climate-related strategies indicates that a bank has good business sense, which is crucial to its client service reputation.

Yet my additional findings on enhanced due diligence show that some leading banks *do* want to influence normative corporate change; however, they will pick the mode of influence on the basis of what is most palatable to them. Due diligence mechanisms do not belie a bank's intention to 'choose' clients on a moral basis, which would compromise the bank's client service reputation and fee generation. Conversely, appearing to choose clients and projects on an economic basis is simply good business sense, which is appropriate and rational. So again we see the double-edged nature of client service reputation: it has the effect of motivating banks a little way down the 'right' path, but also inhibits them going too far.

Lack of Organizational Incentives and Diffusion

The strongest evidence that bank climate-related endeavors are not yet core was that none of the interviewees had salary incentives or key performance indicators ('KPIs') tied to environmental outcomes or mitigation of climate change. Change management scholars argue that sustainability-based thinking and behaviors must be embedded in everyday activities in order to generate real organizational change.[77] Doppelt states specifically that an organization needs to link "bonuses, promotions, new hiring, and succession planning to performance on sustainability" in order to motivate cultural change toward genuine triple bottom line sustainability.[78]

My data show that remuneration and KPIs are not so linked in leading banks. Transactional bankers revealed that their compensation depends on fee generation and how the individual, department, and bank perform financially each year. In some cases there was commission on deals. Yet, the 'greenness' of a deal was not relevant to remuneration: "whether I IPO[79] climate friendly companies or dirty companies I still get paid" (E1). One interviewee asserted that her remuneration was linked to 'carbon'. Yet, after further probing, it became clear that this was due to her involvement in trading carbon as a commodity; it did not equate to a KPI for positive environmental performance or climate change mitigation. Similarly, researcher and analyst compensation was "linked to financial not environmental outcomes" (E2). These employees were judged on their level of external recognition via client and industry voting, which depended on how much their work had added value to client investment and decision-making processes.

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[76] Lundgren and Catasúsm, above n 51, 190.
[77] See, eg, Bob Doppelt, 'Overcoming the Seven Sustainability Blunders' (2003) 14(5) *The Systems Thinker* 2; Bob Doppelt, *Leading Change Toward Sustainability* (Greenleaf, 2010); Derek Smith, 'Engaging In Change Management: Transformation Through Sustainability Strategy at Norm Thompson Outfitters' in Sissel Waage (ed), *Ants, Galileo & Ghandi: Designing the Future of Business through Nature, Genius, and Compassion* (Greenleaf, 2003) 93; Hans-Jürg Hess, 'CSM/WWF Research Project: The Business Case for Sustainability/ Financial Services Sector Report' (Working Paper 2003-8, IMD International, 2003).
[78] Bob Doppelt, 'Overcoming the Seven Sustainability Blunders' (2003) 14(5) *The Systems Thinker* 2, 3.
[79] An Initial Public Offering (IPO) is the first sale of a company's stock to the public. IPOs are used in the renewables/clean tech space as a way to raise necessary capital for a company.

Finally, the KPIs of CSR managers tended to be linked to external recognition and "coalition building" (D2) via CRA government ratings, NGO rankings, and "good sustainability ratings and the resulting reputational impact for the firm" (C2). As such, there was no evidence that banks had heeded Hart's exhortation for companies to "close the loop on their own rhetoric" by rewarding employees that move "the company *and the world* toward sustainability".[80]

Furthermore, attention to climate change, let alone mitigation of it, did not appear consistent throughout the banks. In only two leading banks it was evident that climate change had been elevated to the corporate governance level with senior management oversight and regular meetings of inter-departmental managers to discuss and coordinate climate strategies. As stated by an NGO respondent: "If climate change is not something the CEO reports on then it hasn't arrived at where it needs to be sitting" (NGO-A1).

Importantly, in nearly all cases, interviewees could not explain clearly whether attention to climate change was spread throughout their bank, whether it was consistent between departments, or whether there were future plans for diffusion of climate-related knowledge, practices or mitigation efforts throughout the firm. Most managers could only tell me how their department or division addressed climate change (or even just 'carbon issues') and/or diffused that knowledge.

This situation in practice is in stark contrast to the change management literature on sustainability, which emphasizes that a 'siloed' approach to socio-environmental issues means an absence of change at the core. Studies by Doppelt and Hess evidence the importance of embedding sustainability into everyday practices throughout the whole of an organization.[81] For example, Hess's study of why financial actors adopt green strategies found that "real changes should take place in the core business" if the business case as driver is to generate a positive sustainability impact.[82] In other words, sustainability must become 'built in' to corporate life and not just 'bolted on' to it.

Piecing together the interview data in this study showed that climate-related consciousness was not consistently nor widely-spread throughout a bank in most cases. In some cases it seemed confined to specific departments only. For example, activities within institutional or investment banking divisions usually involved attention to climate change by focusing on carbon as a risk factor or trade commodity, and clean tech as an investment opportunity. Yet this did not seem to be the case for activities in other divisions within the same bank, such as wealth management or retail banking.

One interviewee was able to explain how this worked in practice:

> It's still early days. But to be honest, in Retail Banking, when a person walks into a branch and wants a home loan, we're not interested in the sea level elevation of the property or carbon emissions. In Corporate Lending, we'll check a company's credentials and if we like their business plan then we'll lend the money. In Institutional Banking, that's when we take into account the environmental

[80] Stuart L. Hart, *Capitalism at the Crossroads: Aligning Business, Earth and Humanity* (Wharton School Publishing, 2007) 231–2, emphasis added.
[81] Bob Doppelt, *Leading Change Toward Sustainability* (Greenleaf, 2010); Hans-Jürg Hess, 'CSM/WWF Research Project: The Business Case for Sustainability/ Financial Services Sector Report' (Working Paper 2003-8, IMD International, 2003).
[82] Hans-Jürg Hess, 'CSM/WWF Research Project: The Business Case for Sustainability/ Financial Services Sector Report' (Working Paper 2003-8, IMD International, 2003) 16.

> practices, reputation management, and long-term sustainability of the business. Could we do more? Absolutely. But that's where we are. (G1)

Taking stock of the evidence so far, it is apparent that even leading banks could be doing more to ensure that their climate-related practices are core to everyday business and facilitate real corporate progress toward a low-carbon economy as opposed to tweaking BAU. For example, in addition to enhanced due diligence processes and activity in carbon and clean tech markets, banks could be: linking employee KPIs to climate mitigation efforts; providing preferential lending rates; redlining the most GHG-intense clients and projects; ensuring that attention to climate change and mitigation efforts is present in all departments and under the umbrella of board oversight; and even assessing bank activities by how far they move us toward the 2°C guardrail on global warming. In the words of one NGO representative: "banks shouldn't think this is their contribution to saving the world… What we are looking for is a little bit of ambition and heroism" (NGO-D1).

Yet the honest response from leading banks, as evidenced in my data, is that they see their core business as servicing clients and making money; not saving the world. Pursuit of commercial success can have flow-on effects that benefit the planet, but these are happy corollaries. 'Success' is measured by business case benchmarks. Whether by hard or soft means, an initiative must translate into making money and not losing money for the bank, and employee remuneration is tied to this imperative.

D. CONTRIBUTION TO SCHOLARSHIP AND FURTHER RESEARCH

Overall, there are grounds for genuine concern about how far and fast purely voluntary bank changes can help take us toward a low-carbon existence. Genuine innovations do exist but they are few. The more prevalent actions, such as carbon trading and enhanced risk assessments, fit readily under the umbrella of 'BAU with a lemon twist'. As such, there is credible cause to question the substantive nature of these changes. Specifically, client service reputation is a double-edged sword. It drives banks to adopt green practices that can enhance and protect client service in order to enhance and protect their own profits. Yet, simultaneously, this means that banks will only make rational and conservative changes that do not compromise their client base or potential for profit maximization.

Overall, we can see that the business case drives voluntary corporate change but, simultaneously, impedes change that is far-reaching and expeditious. Business case logic is tantalizing but unsatisfying as an assured modality of corporate change that can facilitate mitigation of climate change.

Accordingly, in the context of stemming dangerous global warming within the next few years, if we relied *solely* on voluntary corporate mainstreaming motivated by business case logic then we would miss a vital opportunity. Importantly, we would miss the opportunity to capture and leverage the full network change potential of the banking industry to facilitate climate change mitigation and the timely shift to a low-carbon global economy. It is clear that the empirical evidence raises normative implications about what we should do now.

An extended analysis of those implications is precluded by the intent and scope of this article; I will dedicate a forthcoming publication to this discrete issue. In short, however, a number of theoretical frameworks can assist analysis at the inter-organizational (meso) and socio-cultural (macro) levels. In particular, two approaches merit acknowledgement here: the first approach focuses on identifying optimal government interventions that mobilize the banking industry for

societal good; the second approach goes beyond existing frameworks to investigate institutional change as an alternative approach to facilitating climate change mitigation. Both of these approaches are described briefly below.

Regarding government intervention, there are two forms that regulation of banks could take in order to facilitate climate change mitigation. The first form is direct 'command-and-control' legislation that mandates how banks must facilitate GHG emissions reductions. For example, legislation could stipulate: that banks must lend at preferential rates to low-carbon industries/projects and at punitive rates to carbon intense ones; or that banks are prohibited from financially supporting listed carbon-intense industries. Clearly, this regulatory approach is strongly interventionist. The advantage of direct regulation is that it sets a high minimum-standard of industry behavior, which might ensure that 'BAU with a lemon twist' is not *de rigueur*. However, critics of traditional regulation, most notably new governance scholars, describe traditional regulation as "hierarchical" and "inefficien[t]",[83] "sanctioned"[84] and "adversarial"[85] due to its coercive nature. Thus, direct regulation (on its own at least) may be ill-equipped to deal with an emerging and complex area like private climate finance that will require adaptation, adjustment and industry collaboration.

An alternate form of government regulation is indirect or 'steering' regulation, which is far less interventionist. Thaler and Sunstein opine that "[t]he sheer complexity of modern life, and the astounding pace of technological and global change, undermine arguments for rigid mandates or for dogmatic laissez-faire".[86] In relation to banks and climate change, it may be more appropriate in market economies for regulators to use indirect regulation to encourage or 'nudge' banks to do what they do best for the good of the planet. For example, policy that incentivizes investment in renewables and low-carbon technology, such as feed-in tariffs and tax credits, stimulates bank finance and broader corporate activity in those areas. If such regulation is long-term and widely spread it has potential to facilitate the private finance necessary to: (a) enlarge low-carbon markets on a scale commensurate to that of traditional fuels; and (b) start up and deploy clean technology on a scale sufficient to move us toward a low carbon global economy. In this way, government regulation exploits business case motivations to make money and not lose it.

Finally, institutional theory may provide important insights beyond theories of the business case or optimal regulation by focusing on the causes of socio-cultural influences rather than their organizational outcomes. Instead of asking 'will a corporation act if the business case is made out?' an institutional theorist seeks to understand the current values framework that shape the requirement for a business case in the first place. Scholars of institutional theory assert that industry or organizational field norms are a product of their macro political-economic context.[87] Organizations allocate resources based on the prevailing macro norm of economic efficiency,

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[83] Jason M. Solomon, 'Book Review Essay: Law and Governance in the 21st Century Regulatory State' (2007-2008) 86 *Texas Law Review* 819, 820, 822.
[84] Orly Lobel, 'The Renew Deal: The Fall of Regulation and the Rise of Governance in Contemporary Legal Thought' (2004) 89 *Minnesota Law Review* 342, 344.
[85] Andrew J. Hoffman and Marc J. Ventresca, 'The Institutional Framing of Policy Debates: Economics Versus the Environment' (1999) 42 *American Behavioral Scientist* 1368, 1375.
[86] Richard Thaler and Cass Sunstein, *Nudge: Improving Decisions About Health, Wealth, and Happiness* (Yale University Press, 2008) 253.
[87] John W. Meyer and Brian Rowan, 'Institutionalized Organizations: Formal Structure as Myth and Ceremony' in Walter W. Powell and Paul J. DiMaggio (eds), *The New Institutionalism in Organizational Analysis* (University of Chicago Press, 1991) 41; Jesse F. Dillard, John T. Rigsby and Carrie Goodman, 'The Making and Remaking of Organization Context: Duality and the Institutionalisation Process' (2004) 17(4) *Accounting, Auditing & Accountability Journal* 506.

which in turn reinforces that norm and the symbolic framework around it. Yet systemic norms can change over time.[88] Hoffman and Ventresca write that "the form of the debate over environmental issues such as climate change is determined by which actors are engaged, what kinds of problems are debated, how those problems are defined, and what kinds of solutions are considered appropriate".[89] DiMaggio and Powell note that interaction between actors in the field can resemble institutional war.[90] And it is at times of conflict that macro institutional (non-isomorphic) change can occur.[91] It must be acknowledged however, that while a 'change the world (literally)' approach is quite exciting from a theoretical perspective, the praxis of *actually* doing so remains complex and challenging.

E. CONCLUSION

Using qualitative interview data from early-moving private sector banks, this study has revealed that change wrought by purely voluntary action based on business case logic is inherently limited, raising serious questions about how far and fast it can help to move us to a low-carbon economy. First, if there is no business case for a climate-related measure, or if there is a competing business case for *non*-green activities (such as fossil fuel investments), then voluntary corporate environmental behavior is stunted. Second, low benchmark-setting by leaders can embed an industry standard that is equivalent to 'BAU with a lemon twist', resulting in incremental and modest change only. The data show that leading banks could be doing more to ensure that their climate-related practices substantively facilitate real corporate progress toward a low-carbon economy as opposed to tweaking BAU.

Central to this conclusion is the discovery that business case logic is a motivator *and* a barrier to corporate green uptake and that client service reputation is a double-edged sword. Importantly, the current size of renewable and clean tech markets is insufficient to entice banks to drop lucrative fossil fuel clients in favor of low-carbon energy clients and solutions. As stated by one banker: "at the end of the day we are not paid to be nice people, we are paid to be successful". (B1). Success is measured by business case standards: make money and do not lose it.

The empirical evidence in this study raises normative implications; it invites scholars and policy-makers to consider how best to mobilize the banking industry to assist timely mitigation of climate change. This task is both challenging and crucial to navigating our transition to a low-carbon global economy.

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[88] Andrew. J. Hoffman, *From Heresy to Dogma: An Institutional History of Corporate Environmentalism* (Stanford University Press, 2001).

[89] Hoffman and Ventresca, above n 85, 1369.

[90] Paul J. DiMaggio and Walter W. Powell, 'The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organization Fields' in Walter W. Powell and Paul J. DiMaggio (eds), *The New Institutionalism in Organizational Analysis* (University of Chicago Press, 1991) 63.

[91] Jesse F. Dillard, John T. Rigsby and Carrie Goodman, 'The Making and Remaking of Organization Context: Duality and the Institutionalisation Process' (2004) 17(4) *Accounting, Auditing & Accountability Journal* 506.