UKSIF
UK Sustainable Investment and Finance Association

Taskforce on Climate-related Financial Disclosures – UKSIF's response

The Taskforce on Climate-related Financial Disclosures (TCFD) was set up by the Financial Stability Board in late 2015. Its mission is to develop voluntary, consistent climate-related financial risk disclosures for use by companies in providing information to investors, lenders, insurers and other stakeholders.

UKSIF submitted evidence to the TCFD during *Phase I* engagement with the private and public sector to review how the financial system could incorporate climate-related issues in financial reporting. Our *Phase I* submission is available here. In December 2016, the TCFD published draft recommendations and launched a public consultation. UKSIF supports the TCFD recommendations and disclosure framework as a vital tool in the transition to a net-zero carbon society which is in-line with the Paris Agreement intended to keep temperature increases to **well below 2°C** above pre-industrial levels and to pursue efforts to limit the temperature increase even further to 1.5 degrees.

UKSIF's response to the TCFD online consultation is summarised below.

How useful are the Task Force's recommendations and guidance for all sectors in preparing disclosures about the potential financial impacts of climate-related risks and opportunities?

UKSIF welcomes the TCFD recommendations. Investors require better, more consistent and more transparent disclosures from companies to enable them to better understand climate-related risks and opportunities. These recommendations represent an important step towards that goal. We are also satisfied that the guidance for all sectors is valuable in setting appropriate context for the recommendations and suggestions for implementation.

Through our discussions with other sector bodies we note a desire from some for more prescriptive measures, with some even advocating the recommended disclosures being made mandatory rather than voluntary. While we remain unconvinced at this stage that approach is practical, we would support the evolution of the recommendations to develop stronger requirements on companies to disclose relevant information in the future.

Linked to this is the concern that, while the recommendations are not at this stage mandatory, not enough emphasis has been placed on current legal obligations for this type of reporting in G20 countries. This risks the possibility of leading some organisations to the false conclusion that this type of climate reporting is always voluntary. While this *specific reporting framework* is voluntary, some G20 countries already have their own legal requirements relating to disclosures of this type, many of which were used to develop these recommendations. The publication could be made far clearer in this respect. We would also expect that increased emphasis of this fact would result in better take up of the recommendations.

Further it is our expectation that, after an appropriate amount of time – and we do not specify how long – this voluntary disclosure framework will become mandatory. This will be essential in driving consistency and comparability in reporting.

How useful is the Task Force's supplemental guidance for certain sectors in preparing disclosures about the potential financial impacts of climate-related risk sand opportunities?

UKSIF welcomes the inclusion of additional guidance for specific sectors in the TCFD publication. We focus specifically on supplemental guidance for the financial sector, in which we were satisfied that insurance firms, asset owners and asset managers have been provided with appropriate guidance.

We felt some concern over the guidance to the banking sector, which has a central enabling role in the economic approach to climate change through lending and other financial intermediary activity. In particular we noted the following footnote:

Recognizing that the term carbon-related assets is not well-defined, the Task Force encourages banks to use a consistent definition to support comparability. For purposes of disclosing information on significant concentrations of credit exposure to carbon-related assets under this framework, the Task Force suggests banks define carbon-related assets as those assets tied to the energy and utilities sectors under the Global Industry Classification Standard, excluding water utilities and independent power and renewable electricity producer industries. The Task Force believes further work is needed on defining carbon-related assets and their potential financial impacts.

Which suggests that further, perhaps substantial, work is needed in this sector. In our discussion with UKSIF bank members opinion was divided: some felt that the guidance for banks was acceptable whilst others wanted more work to be done. At this stage our view is that the lack of a recognised definition of carbon-related assets for use by banks is a major obstacle to the success of these recommendations. Given their voluntary nature, it is unclear how far banks are willing and able to develop a universal understanding of the term. We agree with the TCFD that more work is necessary to define carbon-related assets, and we recommend that it bring together the necessary players to ensure progress continues.

The Task Force recommends organisations describe how their strategies are likely to perform under various climate-related scenarios, including a 2C scenario. How useful is a description of potential performance across a range of scenarios to understanding climate-related impacts on an organisation's business, strategy and financial planning?

Scenario analysis for climate-related risks and opportunities is a relatively recent planning tool. We support the TCFD's recommendation that organisations disclose these impacts on their business, strategy and financial plans under different future scenarios, including a 2° Celsius scenario. We note the following footnote:

'A key type of transition risk scenario is a so-called 2°C scenario, which lays out a pathway and an emissions trajectory consistent with holding the increase in the global average temperature to 2°C above pre-industrial levels. A 2°C scenario provides a common reference point that is aligned with the objectives of the Paris Agreement.'

The Paris Agreement is to keep the global temperature rise this century **well below** 2°C and to pursue efforts to limit the temperature increase even further to 1.5°C. Although the TCFD does reflect this at points in both the recommendations and the guidance, this inconsistency is unhelpful; the publication should be amended to properly reflect the aims of the Paris Agreement.

We appreciate the TCFD recommendations aim to be both ambitious as well as practical for near-term adoption. We would therefore highlight the Client Earth submission which argues that if the choice of 2°C has been made deliberately, perhaps due to a lack of data currently making it impractical to recommend the scenarios the Paris Agreement is geared towards, this should be explicitly acknowledged. In the event that this is the case, Client Earth have drafted an amendment to the text which we fully support.

The Task Force recognises that there are challenges around disclosing sufficient information to allow a better understanding of the robustness of an organisations strategy and financial plans under different plausible climate-related scenarios. Some challenges may arise from unfamiliarity with scenario methodologies and metrics, insufficient practice standards, or cost. What do you view as effective measures to address potential challenges around conducting scenario analysis and disclosing the recommended information?

We need clearer "rules of the road". There are many challenges around disclosure of information to allow investors and other stakeholders to understand an organisation's strategic and financial plans under different climate-related scenarios. Some of this may, as implied, be related to ensuring enough data is disclosed. Equally important is consistency of data disclosed across organisations to enable comparability within a given sector. This is an area in which the recommendations could be strengthened.

The TCFD report states:

In this regard, the Task Force recommends organizations use a 2°C scenario in addition to two or three other scenarios most relevant to their circumstances, such as scenarios related to Nationally Determined Contributions (NDCs), business-as-usual scenarios, or other challenging scenarios.

And:

Organizations with more significant exposure to climate-related issues should consider disclosing key inputs and assumptions related to their scenario analysis to allow users to understand the process and its limitations. In particular, it is important to understand the critical parameters and assumptions that materially affect the conclusions drawn. As a result, the Task Force believes that organizations with significant climate-related exposures should <u>strive</u> to disclose the elements described in Figure 7 (p. 31).

Best practice standards around scenario analyses would be helpful. Self-selection of particular scenarios by organisations will result in inherently inconsistent data and will certainly not result in data which are easily comparable by investors and other stakeholders. We are unsure why organisations with significant climate-related exposures should 'strive' to disclose the elements of their scenario analysis including analysis. Both of these aspects are too weak and should be strengthened.

Part of the Task Force's remit is to develop climate-related disclosures that would enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector. Beyond the metrics included in the Task Force's guidance, and supplemental guidance, what other metrics could be used to measure carbon-related assets in the financial sector?

We think the TCFD recommendations for asset owners, insurers and asset managers are cogent, but as we have noted above the footnote referring to definitional issues in relation to banks needs to be addressed. The issue of definitions can either help this work or hobble it and we urge the TCFD to act in every way possible to ensure it is the former. At this stage we feel there is merit in letting market practice determine the precise metrics that are used once a base-level of agreement is reached. Our interpretation is that that base level has not been reached in banking but has been- or is close- in the other areas.

We urge the TCFD to study the definitions space carefully and flexibly and to react as necessary in sectors and sub-sectors. You should be prepared to "name and shame" groups of interested parties that do not co-operate. You might consider forming industry groups in order to support and further work in this area.

Which types of organisations should describe how performance and remuneration take climate-related issues into consideration?

UKSIF believes all organisations – those in the energy group, as described by the Task Force, financial sector organisations and non-financial sector organisations – should describe how performance and remuneration take climate-related issues into account.

How useful would the disclosure of Greenhouse Gas emissions associated with investments be for economic decision-making purposes (e.g. investing decisions)?

Very useful. We agree with the view outlined by the UK Government following the introduction of the mandatory GHG reporting in 2012. More information is available in the following Government press release https://www.gov.uk/government/news/leading-businesses-to-disclose-greenhouse-gas-emissions

Prior to the introduction of the reporting requirements there was a wide ranging consultation with businesses which outlined that a compulsory approach to GHG reporting would:

- Provide the first step in enabling companies to manage and reduce emissions;
- Mean more transparency from companies;
- Provide a single consistent standard; and
- Provide information to the business that could save them money through reduced energy costs.

These outcomes are beneficial to companies, investors and ultimately savers, and we would expect to see similar benefits to flow as a result of companies implemented the TCFD recommendations.

What additional feedback would you like to provide the Task Force on the recommendations?

We congratulate the TCFD on its work to date. The political climate in which we now operate is changing, but this must not impede the TCFD's important work. Climate Change must be removed from politics, You should act as if it already has been.