

## FSB TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

### PUBLIC CONSULTATION QUESTIONS

#### COVERAGE AND AUDIENCES

**1. Which types of nonfinancial firms should any disclosure recommendations cover? List in order of importance.**

1. Energy (equipment, services, oil, gas, etc.)
2. Utilities (electric, gas, renewables, water)
3. Materials (chemicals, construction, metals & mining, paper & forest, etc.)
4. Industrial (capital goods, commercial services, transport)
5. Consumer Staples (food, beverage, household, etc.)
6. Consumer Discretionary (auto, durables, retailing, etc.)
7. Health Care (equipment, services, pharma, biotech)
8. Telecommunications (diversified, wireless, etc.)
9. Information Technology (semiconductors, software, hardware, etc.)

'Please list any other recommendations'

The Agriculture sector (production, supply chains, etc) is particularly vulnerable to climate risks while also accounting for 15 to 30% of emissions (depending on accounting).

The Technology sector (particularly storage) will lead the charge on making real the transition to a low-carbon world. So those companies also need to disclose what they are doing in this regard (focusing on opportunities not risk).

**2. Which types of financial firms should any disclosure recommendations cover?**

Options: **ALL**

- Banks (diversified, thrifts, mortgage, etc.)
- Diversified Financials (asset management, investment banking/broker-dealer, consumer)
- Insurance (brokers, multi-line, property, reinsurance, etc.)
- Real Estate (REITS, management and development)
- Credit Rating Agencies
- Investment Consultants
- Pension Funds/Schemes

### Other

Private Equity; Endowments; Sovereign Wealth Funds; Infrastructure. From a financial stability perspective, these labels should not matter. If TFCF is concerned about financial sector exposure to climate risks/opportunities, then no asset class should be exempted. If it is concerned about climate related systemic risks, then it should not limit its focus to listed companies. For example, banks have commercial lending to small businesses which together have important macro level impact (employment etc). Requiring disclosure from banks could cause them to speak frankly to all their borrowers about climate risk. The same for investment consultants, auditors, etc.

### **3. Which users in the financial sector should be considered as the target audience?**

- Investors (including insurance, asset managers, funds, pensions, etc.)
- Banks (diversified, commercial, project finance)
- Broker-Dealers and Investment Banks
- Credit Rating Agencies
- Consultants/Advisory
- Other: Financial regulators; Retail investors; Sell Side analysts; ESG analyst; Auditors; Voting advisers

## **2. CLIMATE RISK DIMENSION**

### **4. For non-financial preparers of climate risk and opportunity information, what are the top three key concerns that you would like the Task Force to keep in mind in making our recommendations?**

1. There is overwhelming (97%) scientific consensus that climate change in our time is anthropogenically-induced. This creates systemic risks that are financially significant and growing fast - especially with respect to globally complex supply chains and food production/access - and heightened due to the interaction with societal and political responses.
2. Dangerous global warming will be experienced as extreme volatility in weather, commodity prices, food and water availability/price, and social unrest. This contrasts with what many market participants seem to assume, namely linear change.
3. These systemic risks are unlikely to be contained without forceful action by investors to encourage companies to act now to reduce their emissions and capture opportunities. Yet disclosure of such information is a first step only to achieving substantive change in corporate behaviour and cultural attitude.

**5. For users of climate risk and opportunity information, what are five specific points of information that you wish to secure?**

(1) Governance & aligning corporate purpose with COP21: board members with climate expertise; alignment of KPIs & incentives with 2C transition plans; longest performance horizon for which management is held accountable; climate-related lobbying activity.

(2) Business Continuity Management: <2C scenario stress tests of key assets & material risks (eg supply chains); capex planning (eg. potential financial impacts of technology/policy change). Underlying assumptions (eg GHG targets & future carbon pricing) disclosed. Forward-looking management strategies in different scenarios may reveal corporate intent better than quantitative data.

(3) Innovation: Total enterprise spending on R&D; total spending on low-carbon innovation/energy R&D; energy efficiency strategies. Revenues and net income from low carbon products/services for past 5 years.

(4) Emissions Data: Scope III emissions, mitigation plans for <2C scenario. Interim targets & timelines in accordance with the 'Science Based Targets' approach.

**6. Are there any best practice disclosures of climate risks by companies that you would like to bring to our attention? What specific climate elements of this disclosure would you like to highlight? (Please limit to two examples)**

Using performance measurement, long term incentive design & remuneration to underpin strategic change. Eg. Xcel Energy (USA) has used new metrics & remuneration incentives to align with a lower carbon future and accelerate business model transition. Investors have significant influence over executive pay; they have accepted that the current system is unfit for purpose even in terms of shareholder value.

On reporting of political influence by fossil fuel companies, Shell is significantly better than its peers, providing information on its positions towards key strands of climate & energy policy i.e. carbon taxes. Shell has also clearly detailed:

- the specific climate and energy policies it has been directly engaging with, and the policy outcomes it has been seeking;
- its membership of trade associations that may be influencing climate and energy policy, the association's lobbying positions. For further details see Influence Map's submission.

**7. "Transition Risk" in terms of climate is an evolving term. How would you define this risk? What specific disclosures would help measure it?**

There are 2 types of transition risk: specific and systemic. The former has received more attention.

(1) Specific transition risk is the risk that the impacts of the clean energy transition are not in the price for that company or sector. For example "stranded asset" risk is the possible loss of significant economic value ahead of their anticipated useful life as a result of changes in legislation, regulation, market forces, disruptive innovation, societal norms, or environmental shocks. Coal in general (and Peabody in particular) are good examples, highlighting the conflicts of interests that prevent highly exposed companies from managing these risks well.

(2) Systemic transition risk refers to the disruptive transition to a low-carbon global economy. As we approach the 2C threshold with inadequate mitigation and resilience measures, there will be pressure for emergency responses. Systemic risk should concern regulators, long horizon diversified investors and the public.

**8. Which three sectors do you think are most exposed to climate risks? For these sectors, how are physical, transition and liability risks best measured and reported?**

All sectors are exposed to a greater or lesser degree and there is a complex interplay between different types of risk and different sectors.

Physical risks: infrastructure; real estate; agriculture. Best measured through robust environmental risk assessments which consider their water dependency and risk to water scarcity, as well as exposure to extreme weather events.

Transition risks: energy; utilities; transport (autos, aviation & shipping); Agriculture; Heavy Manufacturing. Please see disclosures on transition risks in Q5.

Liability risks: energy; financial; utilities. Best assessed through a review of disclosures on physical and transition risks, and also governance (board-level) process.

**9. How should the task force consider the challenge of aggregate versus sector-specific climate-related financial risks and opportunities?**

Aggregate climate related risk, better termed systemic risk, can only be mitigated by global action to reduce emissions in line with a below 2C scenario. Therefore all sectors should be asked by their investors to publish below 2C transition plans. When a critical mass of each sector is doing this, first mover disadvantages (eg NRG) will be addressed.

This requires regulator proactivity and know-how. It cannot simply be 'subcontracted' to investors. So the TCFD should consider:

- what scenario information companies and investors need today. The IEA 450 scenario is often referred to as a benchmark 2C scenario, but it does not include the long term targets agreed to in the Paris Agreement to deliver <2C;
- how aggregate supply/ demand numbers are reconciled. Eg. O&G companies may assume coal use declines. Similarly, given the limits on use of oil, it is important to assess the collective assumptions about use made by car, aviation, and manufacturing sectors.

**10. Is there a role for scenario and sensitivity analysis—for the nonfinancial and/or financial sectors? Please provide three specific examples.**

Both approaches have value and for both sectors.

Amongst corporates, market leaders on climate related scenario work include BHP Billiton, Shell & Unilever. The lack of standardised assumptions reduces the value of this work to investors (see our assessment of the BHP report) and the submission by Steven Lydenberg.

It is worth noting that:

- (a) Scenario thinking was more common in the investment system in the 1970s but with the focus on managing narrowly defined quantitative portfolio metrics, this strategic decision making competency has been 'lost' with disuse;
- (b) Investment beliefs can change misaligned investment and stewardship practices. CalPERS and PPGM are two good examples of where this has happened well. Individual thought leaders in the industry (eg Keith Ambachtsheer, Jason Voss) are also promoting scenario thinking. But major educational bodies like the CFA Institute will need to be more engaged to deliver financial sector change.

### **3. ASSET CLASS DIMENSION**

**11. Which are the key asset classes that require initial attention? Are there any gaps that we should focus on? Within this, what are the top two priorities for action? (Limit 1000 characters).**

Options: **ALL**

- Equities
- Fixed Income
- Commodities

Project and Infrastructure Finance  
Real Estate  
Private Equity  
Loans and other bank financing

'Other'

From a financial stability perspective, these labels should not matter. If TFCF is concerned about financial sector exposure to climate risks/opportunities, then no asset class should be exempted.

'Suggested 2 priorities':

1. The TCFD should seek to normalise the idea of <2C transition plans, focusing on the biggest markets and where resistance to change is highest. The USA comes high on both criteria and the SEC could usefully be encouraged to be more proactive on issues not only directly related to climate disclosure but also on corporate influence over political and regulatory decision-makers. See for example the strong advice from Christiana Figueres that: "A key first step in support of the UN Secretary-General's Summit would be for asset owners and managers to request that all companies within their portfolios end the practice of spending shareholder funds on opposing government clean energy policies and action nationally and globally on climate change."
2. Encourage non equity investors in ways that align with their business models.

Fixed Income investors could encourage national governments to implement COP21 agreements and thus also ensure country laggards catch up with leaders. They would be helped to do so if climate risk was fully integrated into core of sovereign debt analysis by credit rating agencies (see pilot work by S&P).

G20/OECD is encouraging infrastructure investing. Much could be done to make this infrastructure a bigger part of <2C transition strategy. See:  
<http://www.ipe.com/analysis/long-term-matters/long-term-matters-followers-will-make-the-money-flow/10011286.article>

With its long-term focus and board control, Private Equity owned companies should be able to move very quickly in producing 2C transition plans. Incentives to do so (eg listing requirements) could help enormously. Those firms which have led on eco-efficiency might naturally want to lead on this phase.

#### 4. INTERMEDIARY/USER SCOPE

**12. Considering the breadth of services the capital supply chain provides, please provide up to three examples of leading work (research or other) from sell-side brokers' investment recommendations, listing rules of stock exchanges, portfolio management and stewardship examples by fund managers, fund-manager recommendations by consultants, or others we should consider.**

1. Aiming for A Investor Coalition: this could be usefully replicated in Canada and Australia. The challenge is to take this “cottage industry” approach to industrial scale. It's only possible with much greater involvement from traditional investor networks (e.g. CII in the USA, CCGG in Canada, Investment Association & Investor Forum in UK, ACSI in Australia)

2. Mercer Investing in a Time of Climate Change: in particular the focus on role of “future makers”. Note: the models use highly conservative assumptions of climate damage functions and stop at 2050 which is when serious systemic risk is likely to manifest.

3. Forceful stewardship: This project adapts the numerical approach used so successfully in the debate on stranded assets to the systemic level. Its 2015 report has now been corroborated by detailed and independent experts (Aviva/EIU, Prof Simon Dietz). It asks investors to go one step further than the robust engagement approach of the Aiming for A coalition by asking for 2C transition plans.

**13. Please identify three examples of existing practice of climate risk disclosures you consider to be effective by investment banks, stock exchanges, investment managers, investment consultants and asset owners? Please indicate preparer and type of disclosure.**

1. SEC mandated disclosure of fund voting shows it is possible to have an evidence-based discussion with managers about their practices (c.f. Australia, Canada or most European countries). See for example analysis of BP's 2015 vote:  
<https://preventablesurprises.com/blog/institutional-investors-carbon-risk-resolutions-dont-sit-on-t-he-fence-please/>

Fund managers & companies access voting information from commercial providers. For greater accountability, regulators ought to ensure civil society groups have similar access.

2. Article 173 of the French Energy Transition Law requires effective disclosures by institutional investors. Engagement is the third pillar. There are best practice examples but no constraints for

the first two years (eg carbon footprinting is optional). Then the regulator is expected to encourage standardisation.

3. SEI metrics project to assess the 2 degree alignment of financial portfolios.

**14. How can climate risk information be simply summarized for retail investors? What standards or mechanisms exist for assuring end investors that climate risks and opportunities have been considered in the way that their savings and investment and pension products have been managed?**

Climate-related risks and opportunities are essentially economic so they ought to be considered in financial reports rather than as a sub-grouping of ESG issues in a 'sustainability' report.

Moreover, a key element for any user (but especially retail investors) is standardisation for comparability.

In most markets, it will be institutional investors that define if systemic risk is well managed or not, so we urge the TCFD to allocate its resources accordingly.

That said, there is much public concern about climate change and this could drive useful change in the system, if 2 major challenges are faced head on:

- (1) Retail investors are easily seduced by data, for example, a benchmark of carbon footprinting scores. But this does not present the full picture. Disclosure must include information on the firm's stewardship policy and practices (in a manner that is comparable).
- (2) it would be misleading for a niche fund to be evaluated alone without considering the impact of the signals sent by the vast bulk of the firm's assets.

## **5. MACRO SCOPE**

**15. In conducting macroeconomic analysis, what are the top three key measures of macroeconomic climate risk performance when seeking to measure the extent to which the global economy is transitioning towards net zero emissions?**

(1) Annual fossil fuel consumption by region; (2) carbon price by region; (3) share of renewables in global generation and of electric vehicles in the global vehicle fleet. Unless and until (1) starts coming down consistently and (2) and (3) are going up sharply the transition is not underway.

Moreover, technology innovation is crucial to a timely transition. So an additional key measure is the pace and scale of investment flows into storage, low-carbon infrastructure, energy efficiency, renewable energy sources, R&D.

**16. One way to measure transition risk is by considering disclosures based on sector/market analysis. What scenario planning work is currently available in this area?**

IEA ETP 2014: a baseline analysis of transition.

IRENA 2015 & various Bloomberg New Energy Finance publications on renewables, electric vehicles & installation of generation capacity.

Mercer's scenarios are a major development: In his forthcoming book, Keith Ambachtsheer welcomes these scenarios saying that they suggest collaboration efforts to secure the Transformation Scenario amounts, arguably, to the "required exercise of fiduciary duty." Experience suggests investors are unlikely to act proactively on this without regulatory intervention.

Addressing systemic climate risk means moving from probabilistic to "possibilistic" thinking. And this means regulators need to explore how they can best influence corporate and investor behaviour. DNB has useful experience in this matter.

[sciencebasedtargets.org/](http://sciencebasedtargets.org/)

CDP's Assessing Low-Carbon Transition Initiative.

**17. The United Nations Framework Convention on Climate Change (UNFCCC) five yearly "global stocktakes" seek to establish in part whether financial flows are consistent with the less-than-two-degree scenarios. Are there any climate-risk disclosure recommendations that would appropriately feed into such an effort?**

Aggregated assets under management (AUM) numbers are often quoted by groups promoting divestment, carbon footprinting, portfolio decarbonisation, climate bonds & also investor membership groups. This growth in green investment is crucial. And we also need to know how proactively investors are helping to reduce 'real world' GHG emissions.

Thus, we consider the most powerful indicator of whether investors are doing what they can is how well they perform as forceful stewards. This will also act as a market pull on intra-firm investment and this is the more significant form of capital allocation today (Kay Review).

In addition, as with countries, the global top 10 investors should report on what they are doing to reduce systemic risk in their portfolios.

See also suggestions in attached paper entitled “Submission to the Financial Stability Board's Task force on Corporate Climate Change Reporting” in particular the proposal to make use of the Know Your Customer framework to stimulate asset owners into action.

## **6. LOOKING AHEAD**

### **18. How should the Task Force define “success”?**

Success in the climate context can only be defined in these terms: we are on track for keeping global warming to below 2C in a timely way.

In practice this means that all firms are forced to consider what a below 2C technology and policy pathway means for their future business/investment plans. Therefore, investors are a key link.

In this context, the USA has the biggest global fund managers and AUM is very concentrated: 6 US mutual fund managers own more than 50% of the shares of the US companies facing climate related resolutions at their 2016 AGMs. If these major investors abstain/vote against, it will be challenging for concerned investors to have positive impact. The SEC has not been as proactive as it might in this debate.

The consequence in short-medium terms: (1) the world's biggest fund managers begin to vote on 2C transition plans due to regulatory interest in systemic risk; and (2) regulators in countries that are important but lagging (eg US-SEC) are persuaded to mobilise and get effective on this issue.

### **19. What are the key barriers that you believe the Task Force needs to overcome?**

Key Barriers:

- Finance theory: long-term investors believe they can ride out climate volatility as with other risks.
- Short-termism: corporate, finance and political.

- Understanding of the risks and opportunities by both finance professionals and also regulators.
- Low support for stewardship amongst investors:  
<https://preventablesurprises.com/blog/how-investors-should-monitor-their-real-world-impact-on-climate-related-systemic-risk/>
- Voluntariness of disclosures; infrequent and inadequate reporting; corporate manipulation of GHG accounting.
- Focus on managing stranded asset risk and assuming this is the same as systemic risk.

Potential solutions:

- TFCD play an educational role (eg speaking about "systemic risk") and encourage peer dissemination of best practice and know-how.
- G20 nations adopt the TFCD recommendations as regulatory requirements.
- Detailed work on how to combat the 'tragedy of the horizons' (supported by the FSB).
- Development of a central repository of asset-level data (see Q.21 below).

## **20. Is the Task Force focused on the appropriate set of topics for its Phase II work plan?**

Yes

## **21. What additional topics should it consider?**

We applaud the TFCD for considering financial opportunities as well as risks in Phase II. Opportunities, if considered in an appropriate time frame, will engage well governed asset owners and also asset managers such as banks.

Specific reporting for Financial Companies is also key. Their key positive impact on systemic risk is to force the pace of <2C business plans. So an important metric for them is voting behaviour. Also important is: a) carbon footprint data (assuming clear & meaningful reduction targets); b) assessments of exposure to green vs brown energy (assuming comparable methodology); c) changes to strategic asset allocation & investment beliefs (to show progressive alignment with COP21 commitments).

In Phase II we recommend exploration of :

- (a) A central climate data repository/portal
- (b) The role of central banks: eg the ECB injects 80 billion Euro into financial markets pm (ie three times average monthly investments into renewables globally).

**22. The Task Force plans to reach out to a broad sample of key stakeholders in the preparer, user and standard setting communities. Are there particular types of entities or organizations that you believe the Task Force should reach out to?**

Recognising the “positive maverick” leadership that has created the TFCF, we encourage consultation with informed individuals to obtain their personal (in addition to organisational) views. Anonymised questionnaires can tap ‘the wisdom of crowds’.

Pilot attempts have been interesting. For example, a Responsible-Investor survey (June 2014) shows that ESG specialists are:

- Very aware of the shortcomings of the investment industry on climate issues (Q2-4);
- Consider a focus on corporate lobbying to be a high impact thing that investors can do (Q8, Q17).
- See their CEOs as not providing strong leadership on these issues (Q9).

See [https://www.responsible-investor.com/images/uploads/articles/RI\\_Divestment\\_Survey\\_.pdf](https://www.responsible-investor.com/images/uploads/articles/RI_Divestment_Survey_.pdf)