# Phase 1 - Survey Response
## For the FSB Task Force on Climate-Related Financial Disclosure

*This document shows the joint response by CDP and CDSB to the FSB Task Force on Climate-Related Financial Disclosure.*

### COVERAGE AND AUDIENCES

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

1. Energy
2. Industrials
3. Materials
4. Utilities
5. Consumer staples
6. Consumer discretionary
7. Information Technology
8. Telecommunications
9. Health Care

The types of companies within scope of the recommendations should be linked to the objectives that the information is designed to support and the outcomes that the TCFD seeks to achieve from the use of information, particularly whether the objectives are to help market participants understand how specific entities are managing climate risk or if the information is designed to serve wider systemic exposures. If the latter, then the types of entities within scope of the recommendations should be much wider. We suggest that the TCFD pursues the approach set out on in the Phase 1 report that recommendations should be aimed at issuers of public securities (non-financial & financial companies).

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

- Banks
- Diversified Financials
- Insurance
- Real Estate
- Credit Rating Agencies
- Pension

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

- Investors (pension, asset managers, boards)
- Broker-Dealers and Investment Banks

### CLIMATE-RISK DIMENSION

4. For nonfinancial 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. The recommendations adhere to the 7 principles of effective disclosure in the Task Force phase 1 report.

2. The Task Force concentrates on building upon current best practice from organisations such as SASB (sector materiality), CDSB (frameworks/standards), and CDP (structure). Recommendations need to include:

- Materiality to that company and sector, with flexibility for the range of risks and opportunities, their time evolution, and the uncertainty of the timing, scale and place of climate impacts.
- Macro exposure - sector and systemic exposures.
- Future fitness - how businesses adapt their business models to be future fit.
- Definitions – ensure a common taxonomy by disclosers AND users.
- Optimized Burden
- Leaders are recognised and laggards pulled to a high standard of disclosure and action.

3. The recommendations demonstrate a pathway of integration into the existing mainstream reporting model

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

- Maximum exposure / assets at risk / revenue at risk
- Risk context & consequence - corrective action including timeframe for remediation, mitigation and adaptation
- New business lines, models and solutions for future fitness
- R&D areas, expenditure and expected revenues for opportunities
- Connectivity – link risk to future development, performance and position, KPIs, management commentary and governance statements

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)

BHP Billiton:
2015 Annual Report – Strategic Report 1.7.2 Risk factors - Climate change may impact the value of our Company, and our operations and markets & 1.7.3 Management of risk factors – outlining their approach to corporate planning, investment decision-making and portfolio management providing a focus on the identification, assessment and management of climate change risks. Identifying the application of an internal price on carbon, scenario planning our portfolio, policy responses and impacts.

BHP Billiton's Climate Change: Portfolio Analysis – providing their perspective on climate change, action on climate change, approach to portfolio management and impacts in a two-degree world.

Other company exemplars from CDP disclosure responses include, but are not limited to, Atos, L'Oreal and Astra Zeneca.

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

This should be the "risk from transition inaction", not "transition risk".
A range of developments, actions & events related to net zero carbon transition in line with a better than 2C pathway which could impact the safety & soundness of firms & stakeholders. Key to successful definition is to define aspects that characterise the transition & pose risks.
To consider:
- All sector risks vs sector, industry or asset specific risks. Research shows that more specific risk disclosures show greater performance-related benefits
- IFRS 9 requires firms to measure expected credit losses of financial instruments using entity-specific & general economic conditions, assessment of current & future conditions
- Clear context for decision making (Carbon Budget) so that firms & investors know the parameters within which they should act, the scenarios against which to stress test & criteria against which their actions will be assessed.
- Progress against <2C pathway, inc. scope 3
- Sensitivity analysis

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

The nature of climate change means that contagion could spread quickly throughout sectors & markets. We note whilst there is merit in additional & specific responsibilities for certain sectors, it is not feasible to restrict scope to 3 sectors.

The most affected sectors are ones whose business models are threatened by: the transition to the net zero carbon economy, impacts of climate change, or whose assets are de-valued or stranded by policy decisions. AMP Capital research “GHG Emissions: Risks & Challenges for Portfolios” indicates Oil, Gas & Coal/Mining, Food/Beverage/Agriculture & Financial Services are most at risk.

Reporting & measurement of these risks includes: litigation, estimate of liability vs. risk occurrence, organisational stress test on carbon price affecting asset value & stranding, reputation & legislation disruption, risk estimation inc. transition & sensitivity to <2C pathways, changes in legislation (e.g. emission limits), adaptation R&D, and insurance claims.

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

The absence of one or more clear objectives means that reporting organisations interpret the objective of climate reporting in multiple ways, leading to variation in the type, quality and quantity of information produced. Disclosers find it difficult to identify material information, as materiality requires judgement to be applied in the light of the reporting objective, users and reviewers of information cannot identify whether it has succeeded in fulfilling the objective of reporting.

Reporting objectives would lead to greater consistency of approach by disclosers, more comparability for users and a set of criteria against which users of information could test intended reporting outcomes. The objective is intrinsically linked to, and should be tested against, decisions made about the audience for the information.

Aggregate information helps the audience understand the inter-connection between sectors, whilst sector specific allows better comparison between similar companies.

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

Scenario and sensitivity analysis is required for both the non-financial and the financial sectors and the task force should consider:

1. Clarifying the context for corporate and investor decision making so that corporations and investors know the parameters within which they are expected to act and the criteria against which their actions will be assessed.
2. Balance of quantitative and qualitative information
3. How scenarios complement forward looking disclosures, governance, risk and corporate reporting beyond 12 month cycles
4. Guidance on the range of scenarios to be evaluated and how to communicate remedial and adaptive actions – e.g. physical affects (e.g. drought, flooding, heat) and legislative by geography
5. Application and alignment with impairment testing (IFRS 6 & 7), disclosure in the notes and sensitivity analysis (IASB's Conceptual Framework (paragraph 4.43)) – as companies identify expenditure and resources not reflected on the balance sheet.

## 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?

Equities

Equity assets would require the initial focus. Equity investors are the first to lose from a downturn in company performance / increase in risk profile. They also have a voice in terms of company management / approach.

Fixed Income

Fixed income is an asset class which often fails to get much focus but is also of importance.

Other

Whilst not an asset class as such, exposure to the different layers of (re) insurance is also a priority.

## 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.

Two sources of research that we would recommend and find valuable are:

- HSBC climate change research.
- Barclays utility work post COP21.

13. Please identify three examples of existing disclosure practices on climate risk and opportunities that you consider to be effective by investment banks, stock exchanges, investment managers, investment consultants, or asset owners. Please indicate the preparer and type of disclosure.

Stranded asset risk – this has had variable levels of useful disclosure so far but analysts try to calculate this and use what companies do disclose to reach conclusions.

2-degree stress testing – an effective way for investors to get a picture of how companies are placed going forward but still not widespread or at a high enough standard. An example is the blueprint from the Carbon Tracker Initiative and Energy Transition Advisors, (http://www.carbontracker.org/report/companyblueprint/) for energy sector companies. This focusses on benefits by assessing 4 common risks across the industry and for individual companies: commodity price risk, demand/volume risk, capital allocation risk, and management risk. This is now being developed further into the Energy Transition Risk project commissioned by the EU Horizon project in March 2016 which will include stress tests.

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?

Emerging approaches to communicate climate risk information of financial products to retail investors focus on the carbon footprint of a fund or portfolio and in some cases its total exposure to companies with proven carbon reserves. However the carbon footprint is a strictly backward looking indicator. Additional data on climate change strategies and sector specific indicators could be summarized and converted into a single, easy-to-use climate change indicator for each financial product.

As of now, only tailored financial products that have a thematic investment approach exist. To engage retail investors in a wide magnitude, will require easy to understand ratings and rankings as they are not aware of Scope 1, 2, 3 details or even 2°.

CDP is tackling this problem in a project with South Pole, University of Hamburg and University of Reading, to develop the first climate rating for all mainstream investment funds, to provide climate transparency to all retail investors globally.

## 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?

We believe that the following provide macro-economic climate risk performance:

- Energy mix – share of renewable energy of the total energy produced
- Indices/share prices of certain sectors and industries by carbon intensity including market capitalization
- Carbon intensity/GDP & Energy / Carbon Price

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

- IEA Scenarios are produced on a country by country basis, based on variables such as national greenhouse gas reduction commitments, whether future policies are made to curb emissions or pathways consistent with a 2C limit on global temperature increase, among others.
- Carbon Tracker Initiative's "The Fossil Fuel Transition Blueprint", fossil fuel industry-specific, based on IEA scenarios

### 17. The United Nations Framework Convention on Climate Change 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?

Reporting on how climate risks are managed, including a target and progress against that target. Some mechanisms for the management of these risks are:

- Internal carbon pricing
- Investments in low carbon / renewable energy
- Evaluating investment in fossil fuels
- Science based targets in line with a less than two degree scenario

These mechanisms may also be reflected in a company's policies.

## LOOKING AHEAD

## 18. How should the Task Force define "success"?

TCFD recommendations are most likely to succeed where they:

1. Are developed to complement existing legal and regulatory reporting requirements and other activities that seek to influence, supervise and regulate the behaviour of organisations in relation to climate change and sustainability more generally;
2. Explain the objective and audience that climate related financial information (CRFI) is designed to serve; what, how and where CRFI should be reported and how to encourage continuous improvement and trust in CRFI;
3. Adopt and enhance current corporate climate reporting requirements and consider the existing corporate (industry led) response to those requirements, as well as evidence from users of information about the usefulness of current reporting practice.

In addition to the above, the TCFD's success is can be measured by:

4. Implementation & uptake across the G20
5. Use by the audience, i.e. incorporation into decision-making
6. Improvements in quality and numbers of disclosure

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

- Identifying what climate info is material & realistic to be reported
- Tension between focusing only on entity specific risks (corporate boundary or value chain) vs on system wide exposures
- Climate change-related reporting extends beyond reporting to the exercise of judgement, accountability & governance practices. New management & governance behaviour must be woven into the fabric of corporate practice.
- Addressing the feasibility of consistency with existing mainstream reporting requirements & practices given focus on liabilities & risks from known events & recognition criteria that exclude certain risks from mainstream reporting
- Absence of definitions
- Distinguishing Climate Related Financial Information from general climate change info & reporting in a way that complements financial info
- Achieving consistency & comparability when many differences in international law & practice exist
- Discrepancy between corporate view & investor view of risk
- Enterprise risk management

## 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?

- Map recommendations with the overview of the current reporting landscape in so far as it requires climate disclosure.

- Provide recommendations on organisational boundary setting for climate-related financial information purposes.
- Develop proposals on the definition and purpose of materiality in disclosure of climate-related financial information.
- Provide a list of resources to which reporting organisations might be referred for help with reporting or associated preparatory activities.
- Develop ideas on how climate-related financial information could be linked or connected with other information in mainstream reports and provide illustrations by way of templates similar to the approach taken by the Enhanced Disclosure Task Force.
- Plans beyond 2016, including a roadmap for the adoption of the Task Force's recommended disclosures

22. The Task Force plans to reach out to a broad sample of key stakeholders among preparers, users, and standard setters. Are there particular types of entities or organizations that you believe the Task Force should reach out to?

- Users of the disclosures: Providers of financial capital. The IASB's Conceptual Framework identifies the primary users of financial reports as existing and potential investors, lenders and other creditors.
- The IASB's Conceptual Framework acknowledges that other parties, including regulators and members of the public, may find general-purpose financial reports useful but they are not the primary users to which general-purpose financial reports are directed.
- Disclosers: financial and non-financial companies such who are expected to report
- Facilitators: financial reporting regulators and other government bodies in charge of setting reporting standards and compliance, as well as non-governmental organisations already in contact such as CDP, CDSB, SASB, CERES, IIRC already involved.