21 May 2021

SEC Headquarters
100F Street NE
Washington DC 20549

Dear Chairman Gensler,
Re: Input on Climate Change Disclosures

The United Nations Environment Programme - Finance Initiative (UNEP FI) is a strategic public-private partnership between the UN and over 400 global financial institutions. It has established some of the most important sustainability-oriented frameworks within the finance industry, including the Principles for Responsible Investment, the Principles for Sustainable Insurance and the Principles for Responsible Banking. It also convenes leading net zero alliances of banks, insurers and asset owners which form part of the Glasgow Financial Alliance for Net-Zero. Since the issuance of the initial TCFD disclosure guidance, UNEP FI has led pilot programmes for dozens of banks, insurers and institutional investors on climate risk and TCFD disclosures. These programs have convened financial institutions, supervisors, and climate experts with a view to improving climate disclosure practices across the financial sector.

The UNEP FI applauds the SEC's decision to evaluate its disclosure rules with a view to facilitating the disclosure of consistent, comparable, and reliable information on climate change. And we welcome this opportunity to share our perspectives on the associated consultation questions accompanying this evaluation process. Our response in particular highlights the following 6 points:

- The importance of mandating the disclosure of climate-related financial risks for both public, but also private firms, to the extent that the SEC is empowered to do so
- The importance of aligning climate disclosure requirements with international reporting initiatives, notably the TCFD standards (including the TCFD's forthcoming guidance on forward-looking metrics) and forthcoming IFRS proposals
- The importance of prioritizing climate risk disclosures, should they come to be integrated into *ESG* risk disclosures
- The importance of requiring firms to disclose scenario analysis as part of quantitative disclosures, with traditional risk measures computed under climate scenarios
- The importance of requiring external verification of climate risk disclosures and including such risks in financial statements
- The importance of learning from the experiences of peer regulators around the world - this for example shows that comply or explain mechanisms can be a useful *starting point* for mandating climate disclosures, with regulatory expectations and supervisory approaches further developing over time, as firms and regulators develop capabilities

Questions

1. How can the Commission best regulate, monitor, review, and guide climate change disclosures in order to provide more consistent, comparable, and reliable information for investors while also providing greater clarity to registrants as to what is expected of them? Where and how should such disclosures be provided? Should any such disclosures be included in annual reports, other periodic filings, or otherwise be furnished?

In terms of the SEC's approach to regulating climate change disclosures, we feel that aligning with international reporting initiatives, notably the TCFD standards and the forthcoming IFRS proposal will be critical to developing comparable and standardized disclosures. There is precedent for such an approach in other jurisdictions.

In the UK for example, the securities regulator known as the Financial Conduct Authority ('FCA') has already introduced a new listing rule and guidance to reflect the TCFD's recommendations as part of a wider commitment by the UK Government to introduce mandatory, TCFD consistent disclosures for actors throughout the UK. This has been achieved through requiring commercial companies with a UK premium listing to include a compliance statement in their annual financial report stating whether they have made disclosures consistent with the TCFD's 4 recommendations and 11 recommended disclosures or providing an explanation where they have not done so. The FCA is responsible for the supervision and enforcement of the above compliance statement and as part of this, is also responsible for monitoring the extent to which companies' underlying disclosures are consistent with the TCFD standards.

The FCA is also intending to consult on both extending its rule to the issuers of standard shares (excluding listed funds) and strengthening the compliance basis for its rule. It will additionally be consulting on bringing forward proposals for asset managers, life insurers and regulated pension schemes to disclose in line with the TCFD. It has additionally publicly voiced support for the IFRS Foundation's proposals.

There are also various other recent European policy and prudential regulatory initiatives[1] that have built on the TCFD standards, some of which we discuss below in the context of the questions on metrics and assurance. The European approach is notable also for its incorporation of the principle of 'double materiality.'[2] This is an approach favoured by the UNEP FI and one that we also encourage the SEC to integrate into its ultimate approach to disclosure.

Finally, on the question of *where* disclosures should be made, our view is that disclosures can/should be included in annual reports as climate risk contributes to other main risk types. However, for clarity, at present, standalone TCFD reports are also helpful.

[1] The European Banking Authority ('EBA') has built on the TCFD's recommendations and is currently consulting on draft technical standards on Pillar 3 disclosures of ESG risks by EU banks with securities listed on regulated markets of any EU Member State. In the EU, the European Commission has also put forward a proposal for an EU-wide Corporate Sustainability Reporting Directive ('CSRD'), which builds on the TCFD, though much of the substantive details are yet to be provided. And in the Eurozone, the European Central Bank has established its Guide on climate-related and environmental risks for banks which sets out its expectations for disclosure in line with the TCFD. This Guide forms the basis for supervisory dialogue with firms.

[2] See for example the Non-Financial Reporting Directive which is to be replaced by the Corporate Sustainability Reporting Directive and see also the EU's Disclosure Regulation, Regulation (EU) 2019/2088.

2. What information related to climate risks can be quantified and measured? How are markets currently using quantified information? Are there specific metrics on which all registrants should report (such as, for example, scopes 1, 2, and 3 greenhouse gas emissions, and greenhouse gas reduction goals)? What quantified and measured information or metrics should be disclosed because it may be material to an investment or voting decision? Should disclosures be tiered or scaled based on the size and/or type of registrant)? If so, how? Should disclosures be phased in over time? If so, how? How are markets evaluating and pricing externalities of contributions to climate change? Do climate change related impacts affect the cost of capital, and if so, how and in what ways? How have registrants or investors analyzed risks and costs associated with climate change? What are registrants doing internally to evaluate or project climate scenarios, and what information from or about such internal evaluations should be disclosed to investors to inform investment and voting decisions? How does the absence or presence of robust carbon markets impact firms' analysis of the risks and costs associated with climate change?

The TCFD's recommendations provide a sound starting basis for the quantification, measurement and disclosure of climate risks through requiring disclosure by firms of:

- Scope 1, Scope 2, and, if appropriate (i.e., where material), Scope 3 greenhouse gas (GHG) emissions, and the related risks
- Metrics used by organisations to assess climate-related risks
- Targets used by organisations to manage climate-related risks and performance against this

The TCFD currently mentions 5 climate risk metrics. However, the TCFD will also be issuing additional guidance on forward-looking metrics for financial firms later this year. Both the current and anticipated guidance should be considered by the SEC.

The TCFD's current suggested climate risk metrics are:

- Weighted Average Carbon Intensity (WACI)
- Carbon Intensity (CI)
- Carbon Footprint (CFP)
- Total Carbon Emissions (TCE)
- Exposure to Carbon-Related Assets

The TCFD also recommends the use of scenario analysis which is something that prudential regulators such as the UK's Prudential Regulation Authority ('PRA') and Eurozone's European Central Bank ('ECB') expect firms they regulate to use on a proportionate basis. The results of scenario analyses should therefore be a part of any quantitative disclosure and traditional risk measures such as probability of default, loss given default, expected loss etc. should be computed under climate scenarios. Disclosures should also specifically include results from *a net zero scenario analysis*.

Firms are also recognizing that risk management alone is not sufficient when it comes to thriving in a climate changed world. Alignment goals and forward-looking targets are important as well. And in this respect, it would also be useful for firms to set out which scenarios their targets are aligned with. Underpinning such commitments are financed emissions data. Firms could therefore use the methodology of the Partnership for Carbon Accounting Financials and Greenhouse Gas Protocol to create consistency across these measures.

Other financial regulatory and legislative approaches to climate risk quantification and metrics that have built on the TCFD framework, with modifications, can be found in:

- The EBA's consultation on draft technical standards on Pillar 3 disclosures of ESG risks by EU banks which proposes disclosure of status quo metrics, including for example, the 'green asset ratio' on EU Taxonomy-aligned activities
- The ECB's Guide on climate-related and environmental risks for banks which additionally proposes disclosure of status quo and forward-looking metrics through disclosure of: carbon related assets (amount or %), weighted average carbon intensity, exposure volumes and credit risk exposures and volumes
- The EU's Disclosure Regulation and accompanying (draft) technical standards

UNEP FI has also produced a best practice/explanatory guide on disclosure of status quo and forward-looking climate risk, alignment and impact metrics[3] for banks and the UK's Climate Financial Risk Forum, has done the same for financial institutions more generally in its Guide. And the World Economic Forum has also produced its Stakeholder Capitalism Metrics.

3. What are the advantages and disadvantages of permitting investors, registrants, and other industry participants to develop disclosure standards mutually agreed by them? Should those standards satisfy minimum disclosure requirements established by the Commission? How should such a system work? What minimum disclosure requirements should the Commission establish if it were to allow industry-led disclosure standards? What level of granularity should be used to define industries (e.g., two-digit SIC, four-digit SIC, etc.)?

In some ways, permitting industry participants to develop disclosure standards reflects the development of the TCFD itself. The initiative was originally a voluntary one that was adopted by the industry. It has formed the core of many mandated climate disclosures in other jurisdictions. However, the mandatory aspect of disclosures is critical to ensure that meaningful and standardized disclosures are provided, giving stakeholders (investors and regulators) decision-useful information.

In our work, we have looked to link together different mapping schemes to ensure comparability. We would recommend ISIC codes as the most common mapping framework. Granularity should be driven by materiality of risk, so some sectors will have further breakdowns than others. Our transition risk methodology and discussion of sensitivities and heat mapping exercise provides further detail on this topic.[4]

4. What are the advantages and disadvantages of establishing different climate change reporting standards for different industries, such as the financial sector, oil and gas, transportation, etc.? How should any such industry-focused standards be developed and implemented?

Different sectors will be exposed to different climate risks. The key indicators in each sector may be different in terms of risk exposure or climate progress. However, despite these differences, a common set of financial standards should exist. As noted above, climate does not stand alone from other risks, but should be incorporated into credit, market, and operational, liquidity and concentration risks.

[3] See in particular, table 3, page 28 for a summary overview of climate disclosure metrics relevant for banks

[4] UNEP FI, Beyond the Horizon: New Tools and Frameworks for Transition Risk Assessments, UNEP FI, October 2020, https://www.unepfi.org/publications/banking-publications/beyond-the-horizon/

5. What are the advantages and disadvantages of rules that incorporate or draw on existing frameworks, such as, for example, those developed by the Task Force on Climate-Related Financial Disclosures (TCFD), the Sustainability Accounting Standards Board (SASB), and the Climate Disclosure Standards Board (CDSB)?[7] Are there any specific frameworks that the Commission should consider? If so, which frameworks and why?

We would highly recommend aligning with international frameworks and standards. The TCFD has become a global de facto reporting standard for climate-related financial risks. While regulators can and have adapted the specific requirements, the pillars and recommend disclosures represent over four years of thinking and iteration about how to report on climate risk. When it comes to standard-setting, the IFRS is working on bringing together the above sustainability reporting initiatives. We would therefore encourage active engagement with these proposals and consideration of the outputs when determining the nature of reporting and the methodologies applied in US reports. Other useful sources that the SEC may wish to consider for the purposes of adaptation referred to above include the EBA's approach to pillar 3 disclosures of ESG risks as per its current consultation and the ECB's expectations as per its Guide

6. How should any disclosure requirements be updated, improved, augmented, or otherwise changed over time? Should the Commission itself carry out these tasks, or should it adopt or identify criteria for identifying other organization(s) to do so? If the latter, what organization(s) should be responsible for doing so, and what role should the Commission play in governance or funding? Should the Commission designate a climate or ESG disclosure standard setter? If so, what should the characteristics of such a standard setter be? Is there an existing climate disclosure standard setter that the Commission should consider?

Disclosure requirements should recognize the current state of companies' capabilities when it comes to climate risk management but should rise over time. The expectation should be that firms devote adequate resources to the identification, assessment, management, and reporting of climate risks. A key area of evolution should be in terms of the granularity of outputs. The growth in both expectations and granularity of outputs as firms build capabilities can also be mirrored in the corresponding approach to supervision.

In terms of responsibility for the disclosure requirements themselves, a key issue will be to ensure that the developer of standards has both the technical expertise and financial resources to be able perform its role effectively. In theory this could be done by the SEC or an alternative body. In the EU for example, the European Financial Reporting Advisory Group (EFRAG) has been selected as the principal architect for the reporting standards that will accompany the EU's Corporate Sustainability Reporting Directive.

7. What is the best approach for requiring climate-related disclosures? For example, should any such disclosures be incorporated into existing rules such as Regulation S-K or Regulation S-X, or should a new regulation devoted entirely to climate risks, opportunities, and impacts be promulgated? Should any such disclosures be filed with or furnished to the Commission?

The key point with regards to climate disclosures is that regulation should require disclosure of decision useful information on climate risks and that the scope of any regulation should be sufficiently wide to capture material climate risks from the various public and private actors within the economy. Any approach to codification should also seek to avoid duplication, be sufficiently accessible and encourage climate risks to be viewed as other business risk types.

8. How, if at all, should registrants disclose their internal governance and oversight of climate-related issues? For example, what are the advantages and disadvantages of requiring disclosure concerning the connection between executive or employee compensation and climate change risks and impacts?

The TCFD's accompanying guidance provides a useful starting point in relation to disclosures on internal governance through requiring disclosure of the following:

Board Oversight of climate risks

- Processes and frequency by which boards and/or board committees (e.g., audit, risk, or other committees) are informed about climate-related issues
- Whether boards and/or board committees consider climate-related issues when reviewing and guiding strategy, major plans of action, risk management policies, annual budgets, and business plans as well as setting the organization's performance objectives, monitoring implementation and performance, and overseeing major capital expenditures, acquisitions, and divestitures
- How boards monitor and oversee progress against goals and targets for addressing climate-related issues.

Management's Role

- Whether the organization has assigned climate-related responsibilities to management-level positions or committees; and, if so, whether such management positions or committees report to the board or a committee of the board and whether those responsibilities include assessing and/or managing climate-related issues
- A description of the associated organizational structure(s)
- Processes by which management is informed about climate-related issues
- How management (through specific positions and/or management committees) monitors climate-related issues.

And the World Economic Forum's Stakeholder Capitalism Metrics further elaborate on this area, including on the topic of remuneration.

In the UK, the Climate Financial Risk Forum has also identified the following as useful disclosure metrics for the purposes of climate risk governance:

- Number of board/committee meetings per year in which climate-related issues have been a substantive agenda item
- Number of events held per year to train board members and management on climate-related issues
- Adjustments to executive remuneration paid during a specific year to reflect performance against specified climate change-related targets

And in the EU, with regards to remuneration, the Disclosures Regulation requires in-scope firms to disclose their remuneration policies and how they are consistent with the integration of sustainability risks more generally.

9. What are the advantages and disadvantages of developing a single set of global standards applicable to companies around the world, including registrants under the Commission's rules, versus multiple standard setters and standards? If there were to be a single standard setter and set of standards, which one should it be? What are the advantages and disadvantages of establishing a minimum global set of standards as a baseline that individual jurisdictions could build on versus a comprehensive set of standards? If there are multiple standard setters, how can standards be aligned to enhance comparability and reliability? What should be the interaction between any global standard and Commission requirements? If the Commission were to endorse or incorporate a global standard, what are the advantages and disadvantages of having mandatory compliance?

We believe that there are significant advantages of developing a single set of global standards which the SEC aligns with. Advantages from this approach include increased comparability and standardization of climate disclosures across jurisdictions. A global standard is also likely lead to a reduction in regulatory costs and burdens imposed on firms as they will not be required to navigate and comply with multiple different standards.

In terms of *which* global standards to follow, as noted above, we favor alignment with the forthcoming IFRS proposals that build on the TCFD framework. With regards to the corresponding standard setter, it would seem that the IFRS would be the natural choice to assume responsibility for this role via its Sustainability Standards Board. And in this respect, we would encourage the SEC to engage with the IFRS individually and via IOSCO, with a view to developing sound global disclosure standards that also reflect the principle of double materiality.

In relation to mandatory compliance, our own pilot programs with financial institutions have demonstrated that learning by doing is an effective way to develop expertise and capabilities in this area. Mandatory compliance is likely to be effective in rapidly accelerating the capacity of firms to identify, assess, manage and disclose climate risks. Limitations in capabilities for example, could, for example be addressed through temporary comply or explain mechanisms and/or approaches to supervision i.e., regulatory forbearance.

10. How should disclosures under any such standards be enforced or assessed? For example, what are the advantages and disadvantages of making disclosures subject to audit or another form of assurance? If there is an audit or assurance process or requirement, what organization(s) should perform such tasks? What relationship should the Commission or other existing bodies have to such tasks? What assurance framework should the Commission consider requiring or permitting?

External verification is already standard for financial statements and for emissions. It is sensible therefore to require third-party verification of climate risk disclosures to ensure that they are accurate and reliable. This will also bring direct benefits to firms themselves through enhanced risk management. Indeed, this is the approach currently being proposed in the EU via the EC's new proposal for its Corporate Sustainability Reporting Directive ('CSRD').

In order to ensure that audits are objective, specific metrics, targets and calculation methodologies will need to be agreed upon that will then be audited. An assurance framework could follow the model that currently exists for financial statements and climate risks should be integrated into financial statements following the establishment of clear expectations and methodologies around disclosures.

11. Should the Commission consider other measures to ensure the reliability of climate-related disclosures? Should the Commission, for example, consider whether management's annual report on internal control over financial reporting and related requirements should be updated to ensure sufficient analysis of controls around climate reporting? Should the Commission consider requiring a certification by the CEO, CFO, or other corporate officer relating to climate disclosures?

Climate controls have been an underexplored area in the global development of climate disclosure guidance. It would be beneficial for the Commission to explore the types of systems and controls that firms should put in place to ensure the reliability of climate disclosures. Certification by a corporate officer could also be valuable once specific metrics and methodologies are agreed.

12. What are the advantages and disadvantages of a "comply or explain" framework for climate change that would permit registrants to either comply with, or if they do not comply, explain why they have not complied with the disclosure rules? How should this work? Should "comply or explain" apply to all climate change disclosures or just select ones, and why?

Comply or explain can be a useful *starting point* for climate risk disclosures while firms build the necessary capabilities (in terms of modelling, analytics and data capabilities) to be able to provide such disclosures. In the UK for example, whilst the FCA has explained that it expects most premium listed firms to be able to disclose climate risks in line with the TCFD's 4 pillars and 11 Recommended disclosures, it currently provides firms with the ability to explain in cases of non-compliance. In such cases, firms are instead required to detail their non-compliance, the reasons for this and their plans to rectify this, along with the intended timescale for rectification. It should be noted that this provision was introduced at the end of 2020 and the FCA now intends to consult on strengthening the compliance basis of these rules, later this year.

13. How should the Commission craft rules that elicit meaningful discussion of the registrant's views on its climate-related risks and opportunities? What are the advantages and disadvantages of requiring disclosed metrics to be accompanied with a sustainability disclosure and analysis section similar to the current Management's Discussion and Analysis of Financial Condition and Results of Operations?

Again, the Commission should follow the work of the TCFD and of global peer regulators (FCA, PRA, ECB and EBA) on eliciting meaningful disclosures. With regards to requiring disclosed metrics to be accompanied with a sustainability disclosure, we feel that climate disclosures can be linked to larger sustainability disclosures provided that the result is greater clarity for a report-reader or stakeholder.

14. What climate-related information is available with respect to private companies, and how should the Commission's rules address private companies' climate disclosures, such as through exempt offerings, or its oversight of certain investment advisers and funds?

A major challenge for financial services firms has been in gathering climate risk data on private institutions. To the extent that it is empowered to set out requirements for non-listed firms, the Commission could explore extending climate disclosure requirements to private companies. Indeed, in terms of global trends, both the Department for Business, Energy and Industrial Strategy in the UK and the European Commission in the EU are currently advancing proposals that would extend disclosure obligations to non-listed companies.

15. In addition to climate-related disclosure, the staff is evaluating a range of disclosure issues under the heading of environmental, social, and governance, or ESG, matters. Should climate-related requirements be one component of a broader ESG disclosure framework? How should the Commission craft climate-related disclosure requirements that would complement a broader ESG disclosure standard? How do climate-related disclosure issues relate to the broader spectrum of ESG disclosure issues?

Unquestionably, nature-related risks and ESG risks are major concerns for corporations today. That said: similar to the answer in question 13, climate risks can be integrated into ESG risk reporting if they do not compromise clarity or generate delays in reporting. The need for prompt regulatory action with regards to *climate risks* is reflected in the approach of several global regulators and policymakers. Regulators such as the FCA and PRA have sought to prioritize climate risks in their approaches due the associated urgency in addressing them. And in the EU, the European Commission proposes prioritizing climate change in the CSDR by adopting a layered approach to its accompanying standards, with the first layer/set of standards intended to cover climate change.

UNEP FI hopes that the answers above will help the SEC to develop its approach to climate change disclosures. We would of course welcome the opportunity to discuss any of these perspectives further or just answer any comments or questions the SEC may have.

Sincerely,

Eric Usher
Director, UNEP-FI