Sustainable finance in emerging markets and the role of securities regulators

CDSB response – 29th March 2019

The Climate Disclosure Standards Board (CDSB) welcomes the opportunity to respond to the Sustainable finance in emerging markets and the role of securities regulators Consultation Report[1] (hereafter referred to as "the Consultation Report").

CDSB an international consortium of business and environmental NGOs catalysed by the World Economic Forum in 2007. We are committed to advancing and aligning the global mainstream corporate reporting model to equate climate change and natural capital information with financial information. We do this by offering companies a framework for reporting climate change and environmental information with the same rigour as financial information. In turn this helps them to provide investors with decision-useful environmental information via the mainstream corporate report, enhancing the efficient allocation of capital. Regulators also benefit from compliance-ready materials. Recognising that information about natural capital and financial capital is equally essential for an understanding of corporate performance, our work builds the trust and transparency needed to foster resilient capital markets.

The CDSB Framework is used by large listed companies globally and is referenced in government guidance to reporting regulation in the EU Commission Guidelines on Non-Financial Reporting, the UK Companies Act 2006, and stock exchange guidance in London, Australia, Singapore, Egypt, Santiago de Chile and elsewhere. CDSB has also contributed to the work of the UN Sustainable Stock Exchanges Initiative through its working groups on disclosure, green finance and financial regulators. CDSB also hosts the TCFD Knowledge Hub on behalf of the G20 Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD), which helps report preparers to find the resources they need to understand and implement the TCFD recommendations.

As evidence of the importance to respond to ESG risks and opportunities at pace and scale grows, securities regulators must play a leading role to address these in order to protect and safeguard the market, investors and society at large. We therefore welcome the recommendations of this Consultation Report, which address many of the key issues to achieve sustainable and resilient financial markets.

Our comments in full are provided below. Please do not hesitate to contact us for further information.

Kind regards,

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[1] https://www.iosco.org/library/pubdocs/pdf/IOSCOPD621.pdf

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Responses to the Consultation Questions

Questions relating to the (Recommendation 1)

1. Do you agree that it is important to include a general recommendation regarding the need for issuers and other regulated entities to integrate ESG-specific issuers in the overall risk appetite and governance?

Yes. Given that the majority of issuers and other regulated entities do not currently take sufficient account of ESG-specific issues, it is important to provide a specific recommendation to highlight the importance of, and the need for integrating these into overall risk appetite and governance.

The lack of sufficient attention to ESG issues results in a less than complete picture of risk exposure, thus affecting the market's ability to price these risks appropriately, in turn affecting financial stability.

There is growing evidence that supports the need for this recommendation. In the case of climate change for example, we draw the attention of the GEMC to research published by the UK's Prudential Regulatory Authority's report on the impact of climate change on the UK insurance sector[2], as well as the report of the European Systemic Risk Board's Advisory Scientific Committee on the transition to a low-carbon economy and systemic risk[3].

This recommendation would promote and contribute to appropriate governance and management of ESG risks and opportunities in Emerging Markets, not only improving their resilience, but improving their attractiveness to international investors by responding to their interest in this topic.

2. Do you have specific comments on the proposed Recommendation 1?

Recommendation could be further improved by amending it as follows:

"Recommendation 1: Integrating ESG-specific issues in overall risk appetite and governance. Issuers and other regulated entities should integrate ESG-specific issues, where these are material *based on scientific evidence and national commitments*, in the overall risk appetite and governance of these entities."

Scientific evidence, such as the Special Report of the Intergovernmental Panel on Climate Change on the impacts of global warming of 1.5 °C above pre-industrial levels[4], provides issuers and other regulated entities with a robust, evidence-based foundation to consider the impacts of ESG issues on their risk appetite. Having a good understanding of their risk exposure can incentivise these entities to ensure that appropriate governance is in place to manage these risks.

In addition to scientific evidence, ensuring that entities are in line with national commitments, such as the Nationally Determined Contributions under the UN Framework Convention on Climate Change or the Aichi Biodiversity Targets under the UN Convention on Biodiversity[5], can safeguard them against the risks associated with the transition to a sustainable economy.

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[2] Bank of England Prudential Regulation Authority (2015). The impact of climate change on the UK insurance sector. [PDF]. Available from: https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/publication/impact-of-climate-change-on-the-uk-insurance-sector.pdf?la=en&hash=EF9FE0FF9AEC940A2BA722324902FFBA49A5A29A
[3] European Systemic Risk Board (2016). Too late, too sudden: Transition to a low-carbon economy and systemic risk. [PDF]. Available from: https://www.esrb.europa.eu/pub/pdf/asc/Reports_ASC_6_1602.pdf
[4] IPCC (2018) Global Warming of 1.5 °C. [PDF]. Available from: https://www.ipcc.ch/site/assets/uploads/sites/2/2018/07/SR15_SPM_version_stand_alone_LR.pdf
[5] UN Convention on Biodiversity (2019) Find National Targets. [Online]. Available from: https://www.cbd.int/nbsap/targets/default.shtml

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Questions relating to ESG-specific disclosures and reporting, and data quality (Recommendations 2 and 3)

3. Do you have specific comments on the proposed recommendation for ESG-specific disclosures and reporting?

We support the inclusion of a recommendation for ESG-specific disclosures and reporting.

We do not however agree that there is a lack of accepted standards. There are a range of widely accepted standards that are in use by issuers and other regulated companies, which address a wide range of stakeholder needs. The Consultation Report refers for example to the recommendations of the Task Force on Climate-related Financial Disclosures, which has been convened by the G20 Financial Stability Board, but has been developed by market participants, for market participants and has gone through extensive consultation processes globally to elicit acceptance by the market and Governments. As a result, more than 580 organisations have expressed their public support of the TCFD as of February 2019[6]. New supporters are added on a continuous basis.

These standards work together at various stages of reporting in order to ensure high-quality data, as well as decision-useful information in mainstream corporate reports. In the case of climate-related financial reporting to a primarily investor audience, a potential approach is outlined in the diagram below:

1. The TCFD recommendations provide a framing of climate-related information, as well as principles and recommended disclosures.

2. The CDP information request helps companies **collect**, **report and structure** their data

3. SASB standards help companies understand what is **material** to their organisation

4. The CDSB Framework helps companies **integrate** the financially material information into their **mainstream filings**

*Please note that this is not a full overview of what each organisation does and there are other reporting standards and organisations that could be included

We also believe that it would be beneficial for the Growth and Emerging Markets Committee's recommendations to refer to the CDSB Framework[7], which sets out an approach for reporting environmental information, natural capital and associated business impacts in mainstream reports, such as annual reports, 10-K filing, or integrated report. It is designed to help organizations prepare and present environmental information in mainstream reports for the benefit of investors. It allows investors to assess the relationship between specific environmental matters and the organization's strategy, performance and prospects.

The CDSB Framework was updated in April 2018 to align with the recommendations of the Task Force on Climate-related Financial Disclosures and other key mainstream reporting requirements, helping to streamline the reporting cycle for many organisations.
Through the provision of robust environmental information, CDSB hopes to encourage analysis and decision-making by investors that recognise the dependence and impacts of economic and financial stability on natural capital.

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[6] TCFD (2019). TCFD Supporters. [Online]. Available from: https://www.fsb-tcfd.org/tcfd-supporters/

[7] CDSB (2018). CDSB Framework for reporting environmental information, natural capital and associated business impacts. [PDF]. Available from: https://www.cdsb.net/sites/default/files/cdsb_framework_2.1.pdf

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The objectives of the CDSB Framework are to:

- Help companies translate their sustainability information into business impacts and long-term value;
- Provide clear, concise and consistent information to investors, connecting the organisation's environmental performance to its overall strategy, performance and prospects;
- Enable and encourage informed investor-decision making on the allocation of financial capital; and
- Add value to an organisation's existing mainstream report, while minimising the reporting burden and simplifying the reporting process.

The Framework also:

- Supports compliance with regulatory reporting requirements with current & emerging requirements for environmental reporting
- Aligns and complements the objectives of financial reporting by providing environmental information that is connected with financial information;
- Aligns with the recommendations of the Task Force on Climate-related Financial Disclosures;
- Builds on the most widely used reporting approaches, such as CDP, GRI, SASB and IFRS;
- Encourages standardisation of environmental information reporting;
- Supports the rigour that is appropriate for information provided to investors;
- Helps prepare assurable reports; and
- The CDSB Framework is complementary to the Natural Capital Protocol.

The development of the CDSB Framework has been overseen by the CDSB Technical Working Group, consisting of representatives from the largest accounting firms, reporting organisations, companies, NGOs and academia.

4. Do you agree that a separate recommendation on data quality is needed? Do you have specific comments on the proposed recommendation?

Yes. While data quality is a core part of reporting, it is worth highlighting it separately.

High-quality data begins before the reporting process. A process for data collection and management must be established within an organisation prior to its actual collection. There are existing processes and platforms in place within organisations that can facilitate this, such as existing enterprise-level and other risk management processes that can be amended to take account of climate risk. Using such existing systems can also support better alignment and interconnectivity between financial and ESG information, allowing companies to manage the two issues in an integrated way, as well as resulting in reporting that provides a more complete picture of the organisation.

While progress has been made in the quality of data available, there is still a concern among data users about the verifiability, consistency, comparability and reliability of ESG data, which is also reflected in Principle 6 of the TCFD recommendations[8].

CDSB, in collaboration with the Sustainability Accounting Standards Board (SASB), has recently published a checklist to help report preparers in preparing for effective TCFD-aligned disclosures. As part of this, some of the items on this checklist apply to high-quality data collection and management[9]:

- Integrate climate change into key governance processes, enhancing board-level oversight through audit and risk committees;
- Bring together sustainability, governance, finance, and compliance colleagues to agree on roles;
- Adapt existing enterprise-level and other risk management processes to take account of climate risk;
- Look at existing tools you may already use to help you collect and report climate-related financial information such as the CDP questionnaire, the CDSB Framework, and the SASB standards;

[8] See Principle 6 on page 53 of the TCFD recommendations, available from: https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-2017-TCFD-Report-11052018.pdf
[9] CDSB & SASB (2019). Checklist: Laying the groundwork for effective TCFD aligned disclosures. [Online]. Available from: https://www.cdsb.net/task-force/895/checklist-laying-groundwork-effective-tcfd-aligned-disclosures

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- Plan to use the same quality assurance and compliance approaches for climate-related financial information as for finance, management, and governance disclosures; and
- Prepare the information you report as if it were going to be assured.

Questions relating to sustainable instruments (Recommendations 4 to 9)

5. Do you agree that this set of recommendations should be applicable to all sustainable instruments, and not only debt instruments?

Yes. While reporting on debt instruments is vital, information on a company's overall governance, strategy, risk management, as well as their metrics and targets relates to other financial instruments, in particular equity. In fact the CDSB Framework, as well as the reporting initiatives outlined on page 11 of the Consultation Report, predominantly focus on the issuer as a whole, rather than a specific issuance of debt or equity.

6. Do you have specific comments on the proposed recommendation relating to the definition and taxonomy of sustainable instruments?

CDSB has no comments on this matter.

7. Do you agree with how eligible projects have been framed in recommendation 5?

CDSB has no comments on this matter.

8. Do you agree that it is useful to have separate recommendations for offering document requirements and for ongoing disclosure requirements, respectively? Do you have specific comments with regard to these recommendations?

Yes. Offering documents provide information that will relate to ongoing disclosure, but provide a different perspective. The two types of reporting are governed by a different set of requirements, which should be reflected in the set of recommendations relating to either.

9. Do you agree that regulators should provide for measures to prevent, detect and sanction misuse of funds raised through the issuance of sustainable instruments?

CDSB has no comments on this matter.

10. Do you agree with the recommendation relating to external reviews? Do you think that such external reviews should be mandatory or voluntary?

CDSB has no comments on this matter.

Questions relating to institutional investors (Recommendation 10)

11. Do you agree that it is important to have a specific recommendation with regard to institutional investors?

Yes. To align financial flows with a sustainable and resilient future, it is important to promote long-term sustainable investment throughout the investment chain. This is also in line with international good practice, such as the EU Sustainable Finance Action Plan[10] and the UK Financial Conduct Authority's recent Climate Change and Green Finance Discussion Paper DP18/8[11].

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[10] European Commission (2018). Action Plan: Financing Sustainable Growth. [Online]. Available from: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097
[11] Financial Conduct Authority (2018) Climate Change and Green Finance DP18/8. [PDF]. Available from: https://www.fca.org.uk/publication/discussion/dp18-08.pdf

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12. Do you agree that regulators should consider asking institutional investors to incorporate ESG-specific issues into their investment analysis, strategies and overall governance?

Yes. In addition to our comment in response to Question 11 above, ESG assessments support a more accurate risk profile, thus supporting more informed decision-making, which in turn benefits institutional investors and savers.

13. Do you agree that regulators should ask the institutional investors to take into account ESG disclosures of the entities in which they invest?

Yes. At minimum, considering whether investments are sustainable or not, including whether they pose certain ESG-related requirements should be beneficial to more informed investment decisions.

Questions relating to capacity building (Recommendation 11)

14. Do you agree that it is important to have a specific recommendation relating to capacity building?

Yes. The past mandate of Securities Regulators has been focused on financial, and more recently, some governance-related matters. Capacity-building is therefore essential to ensuring that these regulators are equipped with the knowledge they require to be able to act effectively, and in the interest of investors and society, on ESG-related matters.

15. Do you also agree that this recommendation should apply both to regulators and market participants?

Yes. While there is some awareness in the market of ESG matters, this is often not formalised through appropriate training. This is certainly the case in relation to reporting, data quality and the supervision of ESG data. As part of its capacity-building work, CDSB will be adding an e-learning section to the TCFD Knowledge Hub this year to provide high-quality training to report preparers on climate-related financial reporting in line with the TCFD recommendations.

Having worked with many IOSCO members, stock exchanges, investors and issuers, CDSB has a proven track record and a wealth of relevant experience of over 10 years of professional education. We would like to explore ways in which we could support the capacity-building work of the GEMC and IOSCO more broadly on the topic of ESG reporting.

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