

Sunday 12 February 2017

The Task Force on Climate-related Financial Disclosures Report Consultation - WFE Feedback

The [World Federation of Exchanges](#) (WFE) would like to commend the Task Force for its work in preparing the disclosure framework and associated recommendations (hereafter referred to as the "[Recommendations](#)"), and the supporting documents (the technical supplements on Implementing the Recommendations and The Use of Scenario Analysis). We believe this work will contribute positively to achieving greater certainty about the type of climate-related information that preparers of financial information should disclose.

The WFE is the global trade association that represents more than 200 Market Infrastructure Providers including exchange groups and standalone CCPs. Of our members, 41 percent are in the Asia-Pacific region, 40 percent in EMEA and 19 percent in the Americas. The market capitalisation of entities listed on our member exchanges is over \$67.9 trillion, and around \$84.18 trillion (EOB) in trading annually passes through the infrastructures our members safeguard.

The WFE works with standard setters, policy makers, regulators and government organisations to support and promote the development of fair, transparent, stable and efficient markets around the world. We share regulatory authorities' goals of ensuring the safety and soundness of the global financial system, which is critical to enhancing investor and consumer confidence, and promoting economic growth. WFE member exchanges also have an abiding interest in the long-term health of their markets and the existence of inclusive and sustainable economies.

The WFE formalised this long-standing interest in and engagement with sustainability in 2014 with the establishment of its Sustainability Working Group. At the end of 2015, the WFE published a set of environmental, social and governance (ESG) metrics and guidance for stock exchanges to use as a reference for promoting sustainability disclosure by listed companies in their markets. The Guidance identifies 33 reporting KPIs based on:

- Exchange guidance (or requirements) already enacted around the world - either by the exchanges themselves, or local market regulators, or reporting frameworks that were most prevalent in a variety of markets;
- The ubiquity of certain indicators across multiple reporting frameworks;
- Investor opinions about the correlation of certain metrics to overall company health, strategic advantage, and/or expected returns as well as increased investor demand for comparable indicators across companies and jurisdictions;
- The research, guidance, and counsel of key investor advocacy groups;
- A reasonable analysis of available resources at companies of all sizes to track and report on these issues.

As operators of stock exchanges, our membership support, and in some jurisdictions, are primarily responsible for requiring and overseeing the disclosure by listed companies of relevant, decision-useful investment information. Perceptions and understanding of what constitutes relevant and material information has changed over time to include ESG information, and most jurisdictions now require at least some disclosure beyond simply

financial information. How this disclosure occurs, and the type of information that must be disclosed, varies across jurisdictions driven by a range of factors including the prevailing regulatory environment. WFE member exchanges are actively engaged with encouraging greater disclosure of relevant ESG issues through a variety of mechanisms, including through listings requirements or through publication of a disclosure guidance to assist companies in their disclosure approach (as just some examples).

In the interests of supporting the work of the Task Force, and enhancing the quality of climate-related disclosure, we submit the following four observations and recommendations for your consideration.

Please note that for the purposes of avoiding confusion in the use of terminology, we use the terms 'ESG' and 'non-financial disclosure' to refer to all disclosure that does not form part of the audited accounts of the company, even though these disclosures may be part of the formal financial report filed for regulatory purposes.

1. Place climate-related disclosures within the context of broader ESG disclosure

We recognise the mandate of the Task Force is to “develop climate-related disclosures that could promote more informed investment, credit [or lending], and insurance underwriting decisions”, thereby enabling an enhanced understanding of the potential financial systemic risk posed by exposure to climate-related risks. We also understand why the FSB has identified climate risk – given its global nature and the recent international commitments in Paris – as the ESG issue that is most likely to be a source of global financial instability. The WFE and its members further acknowledge the importance and urgency of finding collective solutions to the challenges posed by climate change.

We caution, however, that it is important to contextualise this challenge and the resultant Recommendations appropriately. For companies (the preparers), climate change is only one of the many material non-financial issues that they must effectively manage (and increasingly, report on). The Task Force does not, however, acknowledge this explicitly, and we believe it should. The Task Force references the work of the Sustainability Accounting Standards Board (SASB), and highlights existing disclosure/reporting frameworks such as the G20/OECD Principles of Corporate Governance, the GRI G4 Sustainability Reporting Guidelines and the IIRC <Integrated Reporting> Framework, all of which identify a range of issues that companies should consider and report against.

To take just one example, SASB identifies five areas (Environment, Social Capital, Human Capital, Business Model & Innovation, and Leadership & Governance) that may pose material financial risks for companies, and proposes relevant disclosure metrics accordingly. The Task Force further identifies the “relationship to other reporting initiatives” as an “area for further work”. Our concern, however, is that by not explicitly contextualising climate change disclosure within ESG disclosure more broadly, these Recommendations become ‘just another framework’ against which companies are required to disclose, potentially undermining the work of the Task Force.

Proposal: In the interests of avoiding the continued silo-ing and fragmentation of the nonfinancial information that companies disclose, the Task Force should more explicitly contextualise the Recommendations within the broader ESG context and existing disclosure framework, thereby acknowledging that climate change information forms a portion of the investor-relevant information that companies are encouraged to disclose. The Task Force may also wish to work with the relevant disclosure bodies and preparers who disclose according to these existing disclosure frameworks, to produce working examples of how reporting against the Task Force Recommendations would fit into these existing frameworks.

2. Allow for a phased approach to implementation of the Recommendations

Stock exchanges are often primarily responsible for requiring and overseeing the disclosure by listed companies of decision-useful investment information. Thus, we believe that we have relevant perspectives to share on the difficulties in implementing the disclosures, or on the factors that would encourage adoption. We therefore submit that:

- “the time and cost of collecting the information”;
- “lack of experience with concepts and methodology”; and
- the fact that “multiple climate-related reporting frameworks currently exist”

are potentially serious impediments to implementing the Recommendations.

We deal with point three (multiplicity of frameworks) earlier in our response. Elaborating on points one and two, while the Recommendations focus on disclosure, the ability of companies to make the recommended disclosures is dependent on the adoption of certain oversight, measurement and assessment practices within the disclosing organisation. This requirement to adopt new assessment practices is not unusual for (particularly non-financial) disclosure frameworks. What is noteworthy about these Recommendations specifically, however, is both their scope and the proposal to adopt a particular approach to modelling climate-risk and associated strategic planning, namely scenario analysis.

Looking first at the proposed use of scenario analysis, while it is presented only as a suggestion, some of the recommended disclosures are tied explicitly to scenario analysis (ref Strategy – Recommended Disclosure c). We agree that when done well, scenario analysis could be an enormously useful tool for strategic planning, and the disclosed results could be of interest to the various users of the information. We caution, however, that good scenario analysis is not easy to do, and requires significant commitment of time and resources. This ‘difficulty’, when coupled with the extensive nature of the Recommendations, (covering almost every aspect of how an organisation thinks about its business), suggests a low likelihood both of preparers adopting the Recommendations, and potentially, even where adopted, of achieving meaningful, decision-relevant information for investors.

Proposal: The Task Force should consider restructuring the Recommendations, to provide for a staged implementation approach. The Task Force could position the full disclosure framework as the desired end state, but then identify interim steps to achieving this. This could include detail on what information they recommend companies disclose as soon as possible (the baseline), versus what they aim to disclose over time, as the preparers become more sophisticated in their understanding of climate risk and opportunities. Initial disclosure recommendations may include information that describes the company status quo as it relates to climate risk and any key metrics that investors/underwriters agree are critical (such as Scope 1, 2 and possibly 3 emissions). As part of this, the Task Force should work with users to identify:

- What information is already disclosed through existing frameworks;
- The usefulness of this information;
- If useful, the quality of the current disclosure;
- Any information gaps in the existing frameworks.

Existing disclosure data points that appear consistently across frameworks, and which users agree are necessary for investment decisions and assessing the carbon intensity of their portfolios, could form part of the desired baseline disclosures. Other information that is necessary for achieving the Task Force objectives, but which does not form part of any current framework and/or may be costlier for the company to report on effectively, should form part of

the aspirational disclosure state. We believe that this more granular and phased approach would both increase the likelihood of adoption of the Recommendations, and obtaining more decision-useful disclosure from the outset.

3. Make the case more clearly to the preparers of disclosure information

On our reading of the Recommendations, it is not completely clear who the target audience is. The stated intent of the Recommendations is to “enable stakeholders to better understand the concentrations of carbon-related assets in the financial sector and the financial system’s exposure to climate related risks”. The Recommendations and their importance are therefore situated within the potential impact of climate change on the financial sector. While this is understandable given the remit of the Task Force, there is very little in the Recommendations that makes a compelling case to the preparers of the information as to why they should be thinking about these issues or disclosing this information.

As mentioned above, the Recommendations impose a non-neutral disclosure burden on companies requiring them to undertake varying degrees of implementation effort. The statement that providers of capital and risk underwriting are increasingly demanding such information could be sufficient to compel companies to disclose the information, but it is not clear that this is in fact currently being factored into capital pricing or underwriting decisions, or if it is, that this is being effectively communicated to companies. In the absence of these market signals, and/or explicit requests for disclosure by investors and debt or equity analysts, more should be done to convince companies of the benefit to them of investing in understanding and mitigating climate-related risks and opportunities. Effectively making the case for change is necessary both to encourage disclosure, and to enhance the quality of the disclosure.

Proposal: We believe that the Recommendations would be improved if they more clearly articulated the potential risks and opportunities of climate change for the preparers of the disclosure, and the associated link to the mandate of the Task Force.

4. Acknowledge the scope of the Recommendations and the cost-benefit challenge more clearly

We conclude with one final observation about the Recommendations. We do not have a specific proposal for these but rather wish to leave this as a general thought for the Task Force to consider. This observation derives from the perspective that exchanges have, given their role in balancing the needs of issuers of, and investors in, public capital.

Flowing from the point we made at the outset about the need for context is an observation about how one meaningfully assesses the relevant costs and benefits of the requisite disclosure. The Recommendations note that “any disclosure recommendations by the Task Force...would need to weigh the balance of costs and benefits”. It is not apparent exactly how this was applied in relation to the eventual Recommendations (and the Task Force may consider articulating this more clearly) but more broadly, the actual cost-benefit assessment relates not to these disclosures in isolation, but to these disclosures in addition to the range of other information that companies are required to disclose.

We would caution that simply requiring companies to disclose more information without assessing the overall disclosure burden not only reduces the likelihood that companies will disclose but - to the extent that many disclosure standards are targeted at listed companies specifically - may actually serve to undermine the relative attractiveness of public markets, resulting in a much broader reduction in corporate transparency.

We would therefore ask the Task Force, as it reviews the Recommendations in light of comments received, to consider very carefully what information is actually required to achieve the stated objectives.

[You can read the related WFE press release here.](#)