Climate-related Financial Disclosures: Understanding Your Business Risks and Opportunities Related to Climate Change

Discussion Document – Comments

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Introduction

My background includes:

- Chartered Accountant and business adviser (30 years), and writer (sustainability and business issues): From the early 1990s I had been concerned that NZ accountants and business leaders had considerable power but lacked understanding of environmental and social issues and the outcomes of their actions. Resulting involvements included:
- Being appointed principal writer and reviewer (part-time) on sustainability issues for 'Chartered Accountants Journal' (1991 to 2004). Articles also in about 15 other local or overseas periodicals.
- Judge and Convenor of NZ Awards for Sustainability Reporting by companies, councils and other organisations, 1995 – 2003.
- Publication (jointly with KPMG) of *Accounting for a Clean Green Environment* (1999); 180 page book, then acknowledged as the authoritative guide to accounting for environmental and sustainability issues in NZ. Supported by Ministry for the Environment with endorsements from politicians (and contributions from Sir Geoffrey Palmer and Simon Upton), business leaders and NGOs.
- Appointed to two NZ Institute of Chartered Accountants national advisory committees on 'sustainability reporting', 2000 - 2004.

This initiative of the government, along with other recent initiatives, is greatly welcomed.

Questions shown are from the Discussion Document. Those on which I have no view, or no strong or sufficiently clear view, have been shown as 'NC': No Comment.

Submission

Chapter 1

Q.1 Is the TCFD reporting framework the most appropriate framework for New Zealand?

It is an appropriate framework, and implementation is urgent. Climate issues are going to be extremely relevant to the NZ environment, society and economy in coming decades – starting right now. World-wide, we are only now beginning to grasp how crucial these are going to be to every aspect of our lives. It is vital that the right information is widely available so that investment decisions are made which are appropriate to our futures.

It is important, though, that the group required to report/explain be broadened to include all kinds of entities, such as large private companies, trusts, cooperatives, overseas listed or owned companies and partnerships.

Q.2 Do you agree with the conclusions we have drawn at the end of chapter 1?

48. We have drawn the following main conclusions:

48.1 Climate change presents material financial risks, both transitional and physical, to many businesses.

Yes. Risks are likely to become apparent very rapidly over the next decade and beyond. These will be not just from physical impacts (e.g. heat and drought) but also a result of growing compliance costs (e.g. a result of increasing ETS and 'Carbon Zero Bill' costs), and from major disruption particularly in overseas countries (e.g. a result of mass migration and changing legislation).

48.2 Responding to climate change presents investment opportunities in areas such as: renewable energy, energy efficiency, adaptation of infrastructure, and land use in farming and forestry.

Yes, countries such as NZ can benefit from being ahead of the pack in developing mitigation and adaptation solutions, particularly related to agriculture, horticulture and marine products. Examples include methane reduction measures for livestock, and use of biochar. However we cannot expect future growth to continue in line with recent decades. There are few areas in which growth does not result in additional climate impacts.

48.3 Climate change is not material to every company of scale. However, it is not possible to know that without first testing the proposition.

Agree.

48.4 Businesses that identify and manage material climate-related information will be better placed to manage risks and seize opportunities.

Yes. Identification and measurement are essential precursors to good management. In many cases, those which do not do so will be rejected by customers or excluded from supply chains.

48.5 Capital will be allocated more efficiently and profitably if entities disclose material climate-related risks and opportunities to investors.

Yes. Climate change, as Sir Nicholas Stern noted in 2006, is the greatest market failure the world has ever seen. Greater transparency around risks and opportunities will help, to some extent, to correct this. One essential for the market to function correctly is to have the right information provided - consistently and comparably.

48.6 Pressure is building from institutional investors for companies to make climate-related disclosures, and is likely to continue to increase.

Yes, this will increase. Disclosure is essential to help to offset market failure. This will build rapidly as understanding of the urgency of climate action is understood, and as a younger generation (including those involved in or influenced by the School Strikes for Climate) enters the market and the labour force, and makes their preferences, concerns and growing anger known.

Chapter 2

Q.3 Do you agree with the objective as set out above?

Yes. However, note that the best information is not always 'financial' information'. Non-financial reporting is often a key component of reporting for corporates and other organisations. And the 'effects' of an organisation might sometimes be far more significant than just the financial effects.

Q.4 Should other objectives also be considered?

Yes, other key sustainability objectives should be considered in parallel with those outlined. It would be useful to link reporting to other measures, for example the Government's Wellbeing Budget and Treasury's Living Standards Framework, and the reporting entity's impacts on vital national assets such as the quality of our water, air and soil.

Q.5 Do you agree with the problem definition? Are there other aspects we should consider?

The 'problem' is broader than just the lack of information in financial markets. Businesses and other organisations also need to earn and continue to justify a social 'licence to operate'. Their objectives, it has now been widely recognised in NZ and overseas, must be wider than just return on shareholder investment. In August this year, for example, the USA Business Roundtable Business Roundtable announced the release of a new Statement on the Purpose of a Corporation signed by 181 CEOs who commit to lead their companies for the benefit of all stakeholders – customers, employees, suppliers, communities and shareholders. These stakeholders also require accurate, timely and comparable information, in order to judge an organisation's performance. Certainly a key part of this is climate-related; all stakeholders have a vital interest in impacts which will affect the very survival of human society and ecosystems.

Chapter 3

Q.6 What are the implications of section 211 of the Companies Act 1993 for the disclosure of material climate-related information in annual reports?

The envisaged reporting should not be limited to entities outlined in section 211 of the Companies Act. See Q. 1 above.

Q.7 What are the implications of the NZX Listing Rules for the disclosure of material climate-related information by (a) equity issuers, and (b) debt issuers?

NC

Q.8 How should proposed adaptation reporting under the Climate Change Response (Zero Carbon) Amendment Bill and the climate-related financial reporting disclosures proposed in this discussion document best work together?

These will need to be closely aligned for compatibility and comparability.

Chapter 4

Q.9 Do directors' legal obligations in New Zealand result in consideration, identification, management and disclosure of climate-related risks?

Currently this is not sufficiently clear. The requirements need to be specifically outlined in legislation.

Q.10 Do you agree with the legal opinion prepared for the Aotearoa Circle?

NC

Chapter 5

Q.11 Do you favour the status quo or new mandatory disclosures?

Disclosure must be mandatory! Many companies will lobby for voluntary disclosure, and will then ignore this requirement.

For nine years I was Judge and Convenor of NZ Awards for Sustainability Reporting by companies, councils and other organisations (1995 – 2003), run in conjunction with the (then) Institute of Chartered Accountants NZ. During that time, the best (and those reporters with little to hide) got better.

The rest did nothing. Poor performers (environmentally) have no incentive to report and highlight their poor performance, unless it is mandatory for them to do so.

Over a number of years I advocated in several NZ publications for mandatory environmental disclosure. This was never enacted. The environment, transparency and the quality of NZ reporting suffered or did not advance as many had hoped in this period. The need is now far more urgent.

Q.12 If a mandatory approach is adopted, do you agree with the Productivity Commission that a mandatory (comply-or-explain) principles-based disclosure system should be adopted?

Yes, and the 'explain' responses would need to be monitored for validity.

Q.13 If the status quo is retained, how can government and investors be confident that risks would be routinely considered in business and investment decisions?

These could not be confident under the status quo. The market failures would continue, to the detriment of the market and the 'climate'.

Q.14 Do you consider the TCFD framework to be best practice in relation to climate-related financial disclosures?

Yes, this may be the best available but continual review and improvement will be required. There may be significant climate-related risks that cannot easily be quantifiable in financial terms. These could include, for example, reputational risks for a company with damaging products or practices that could result in it being black-listed or boycotted by angry investors or consumers.

Q.15 What are your views about whether the TCFD's recommended disclosures will provide useful information to institutional investors and other users?

These will be a useful but incomplete source of useful climate-related information.

Consistency between reporting entities will be important for comparability.

Q.16 Do you think the proposed disclosure system will encourage disclosing entities to make better business decisions?

Yes, absolutely. Many companies have been totally unaware of their impacts until they measured and disclosed them. Some have been so shocked by results that they have pledged publicly to 'clean up'.

Q.17 Is the definition of materiality in the IASB Conceptual Framework for Financial Reporting appropriate for this purpose?

This is a reasonable starting point. It would be useful for impacts to be reported qualitatively anyway, if not quantitatively. Some may underestimate likely costs or impacts, so disclosing the nature of these will at least allow the market to make an assessment.

One such example could be stranded assets (such as oil not yet extracted, but which should never be extracted due to growing climate risks). It's certainly an area where there could be big differences of opinion between those that hold such assets, and others who might consider them to have nil value.

Q.18 What comments do you have on our proposal that non-disclosure would only be allowable on the basis of the entity's analysed and reported conclusion that they see *themselves as not being materially affected by climate change, with an explanation as to why?*

I believe we should avoid such exceptions – it's a loophole which might attract considerable efforts to exploit.

Some entities might see themselves as not being materially affected but they might in turn have considerable climate effects on others – a company drilling for off-shore oil or a corporate dairy farm, for example.

Q.19 What are your views about providing a transition period where incomplete disclosures would be permissible?

This needs to be minimal. Climate issues are now very urgent.

Q.20 If there is to be a transition period, what are your views on it being for one financial year?

It should certainly not be greater than one financial year.

Q.21 Should all of the following classes of entity be subject to mandatory (comply-or-explain) climate-related financial disclosures: listed issuers, registered banks, licensed insurers, asset owners and asset managers?

Yes.

Q.22 Should any other classes of entity be required to disclose?

Yes, see Q. 1.

Q.23 Should there be an exemption for smaller entities?

Yes, but very limited.

Q.24 If there were to be an exemption:

(a) What criterion or criteria should be used: annual revenue, total assets, a combination of the two, or some other measure or measures?

GHG impacts should also be considered.

(b) Which dollar amount or amounts would be appropriate?

NC

(c) Should there be a requirement to adjust for inflation from time-to-time?

Yes.

Q.25 What are your views about our proposal to have a stand-alone climate-related financial disclosure report within the entity's annual report?

It is better for this to be integrated in one report, so the information cannot be missed.

Q.26 What are your views about providing for disclosing entities to include cross-references or mappings within that report to assist users to find relevant information?

This would be useful.

Q.27 What are your views about requiring explanations for non-compliance to be included in the annual report?

Explanations should be included and suitably verified.

Q.28 Should there be mandatory assurance in relation to climate-related financial disclosures?

Yes.

Q.29 Which classes of information should be subject to assurance if it were to be mandatory?

All items which are considered to be material.

Q.30 Do you consider that assurance should be required in relation to GHG emissions disclosures?

Yes!

Q.31 Is limited assurance the only practicable approach in relation to TCFD disclosures, or is reasonable assurance also feasible?

NC

Q.32 If we do not introduce mandatory assurance when a disclosure system comes into effect, should it be reconsidered in the future?

Yes, within a limited time, perhaps 3 years.

Q.33 What comments do you have on the proposal to bring the disclosure system into force for financial years commencing six months on or after the date that the regulation is introduced?

Yes, this reflects the urgency required.

Q.34 Do you consider that smaller entities should be provided with a longer transition if there were to be no exemption for them? If so, how long should that additional period be?

Yes, perhaps one to two years.

Q.35 Do you have any views about the legislative means for implementing new mandatory (comply-or-explain) disclosure requirements?

NC

Q.36 Do you consider that there is a role for government in relation to guidance, education, monitoring and reporting?

This is probably best done by other providers.

Q.37 Are there other activities that a government agency could usefully carry out?

NC

Q.38 Which government agency or agencies will be best able to carry out these functions?

NC

Q.39 What would you need to assist you with a full set of TCFD disclosures?

None.

Q.40 What information do you have about the cost implications relating to these proposals?

None.

Q.41 What information do you have about costs for specific types of reporting entities?

None.

Q.42 Do you have any other comments?

The proposals are necessary to correct major market failures, and are urgent and overdue. Climate change impacts will be seen and felt very rapidly over the next decade and beyond. This is one more mechanism that will help to slow these impacts, by informing investors and others, who might then choose to not to support or invest in these activities.

In general terms, I support the proposals but believe that in some areas these need to go further and faster.

Thank you.