Climate Finance Fund

July 28, 2022

VIA ELECTRONIC FILING

International Sustainability Standards Board (ISSB)
Emmanuel Faber, ISSB Chair
Sue Lloyd, ISSB Vice-Chair

Re: Exposure Drafts IFRS S1 General Requirements and IFRS S2: Climate-related Disclosures

Dear Chair Faber and Vice-Chair Lloyd,

We welcome the publication of exposure drafts IFRS S1 and IFRS S2 by the ISSB and are encouraged by the acknowledgement of investor needs for improved climate and sustainability-related disclosures.

The Climate Finance Fund manages a $US 75 million + portfolio mobilizing capital for climate solutions across China, the United States, and parts of Europe. We focus on venture capital, bank lending, and asset management. The Fund finances everything from new climate-friendly investment products to investment funds, as well as funds systemic climate finance action using financial regulatory mandates. All of our work has a justice, equity, diversity and inclusion (JEDI) lens. This is the context within which we submit our comments.

We applaud the requirements to disclose Scopes 1, 2 and 3 absolute emissions, climate-related opportunities, the use of internal carbon pricing, the presence and nature of climate targets, and how climate-related considerations are factored into executive remuneration.

Nevertheless, the current exposure drafts do not fully account for the needs of all investors, including retail investors that invest for retirement savings at a longer time horizon and investors that deploy climate impact and justice strategies. The current ISSB exposure drafts do not set a global baseline for the world's investors that hold at least $US 35 trillion in assets and growing.[1] **To remedy this, we encourage the creation of a single set of standards to meet all investors needs coordinated between the ISSB and the Global Sustainability Standards Board (GSSB).**

Below are our suggestions to enhance the draft standards' ability to deliver high-quality climate disclosures that provide ***all kinds of*** investors with information about the climate-related risks, opportunities and impacts of a company.

[1] ESG by the Numbers: Sustainable Investing Set Records in 2021.
https://www.bloomberg.com/news/articles/2022-02-03/esg-by-the-numbers-sustainable-investing-set-records-in-2021

1. Governance of the ISSB

We start with the foundation of sound sustainability policy, including climate-related disclosures: governance. In order to create a trustworthy and credible global baseline, the governance structure of the ISSB itself must evolve. According to the IFRS Foundation Constitution, the ISSB membership shall be composed as follows:

> *In a manner consistent with the 'Criteria for ISSB members' as set out in the Annex to this Constitution and in order to ensure a broad international balance, there shall normally be:*
> *(a) three members from the Asia-Oceania region;*
> *(b) three members from Europe;*
> *(c) three members from the Americas;*
> *(d) one member from Africa; and*
> *(e) four members appointed from any area, subject to not creating overall geographical imbalance.*

It is not clear to us which criteria have been used to calculate the proportions reflected in the geographical distribution of membership positions above. In any event, we are of the firm opinion that geographical balance cannot be achieved by assigning only one member from Africa, a continent of over 1.2 billion people, containing over 30% of the world's mineral reserves (which are all-important for climate solutions), home to several of the world's fastest-growing economies,[2] and that will experience some of the most disproportionate impacts if climate justice is not achieved.

The current governance also lacks a geographic breakdown that illustrates the complexities and realities of corporate presence, mergers and acquisitions, and supply chains. The lack of specificity could also lead to significant overrepresentation (for example, three members from the Americas could easily emanate from only one country). We would suggest a further breakdown that represents economic and thus corporate clusters, such as CARICOM, ASEAN, and EAC. This would ensure a truly inclusive, and therefore trustworthy, set of global baseline standards.

We consider diverse, balanced representation in the ISSB's composition to be an essential component in guaranteeing its credibility, and by extension that of the Exposure Drafts themselves. **We would therefore encourage the IFRS to a) clarify the methodology used and b) modify the seat allocations to be diverse and inclusive.**

[2] https://www.imf.org/en/Publications/WEO/Issues/2022/01/25/world-economic-outlook-update-january-2022

2. Impact

The ISSB focus on sustainability-related risks and opportunities in relation to enterprise value must recognize that these risks and opportunities arise from both an entity's impacts and dependencies on people and the planet. The climate-related disclosures must therefore address the climate-related, including climate justice, impact of a company's business activities across its value chain. We would suggest a simple change:

Throughout the Exposure Draft, replace "climate-related risks and opportunities" with "climate-related risks, opportunities and impacts."

3. Compatibility with a 1.5°C pathway

It is essential that the Exposure Draft contains clear and unambigious recognition of the need for reporting entities to work toward achieving compatibility with a global temperature increase pathway not exceeding 1.5°C as is currently outlined in the draft ESRS.

At present, the ISSB Exposure Draft refers only to the objectives set out under the "latest international agreement on climate change," i.e. limiting global warming to "well below 2 degrees Celsius above pre-industrial levels."

We recommend the following:

Insert reference to 1.5°C alignment under "Objectives" (p. 32):

> The objective of IFRS S2 Climate-related Disclosures is to require an entity to disclose information about its exposure to significant climate-related risks**,** ~~**and**~~ opportunities, **and impacts**, enabling users of an entity's general purpose financial reporting:
>
> > to evaluate the entity's ability to adapt its planning, business model and operations to significant climate-related risks**,** ~~**and**~~ opportunities, **and impacts**, **in order to become compatible with limiting global warming to 1.5°C.**

Insert references to 1.5°C alignment under "Metrics and targets" (p. 40):

> The objective of climate-related financial disclosures on metrics and targets is to enable users of general purpose financial reporting to understand how an entity measures, monitors and manages its significant climate-related risks**,** ~~**and**~~ opportunities, **and impacts**. These disclosures shall enable users to understand how the entity assesses its performance, including progress towards the targets it has set **in order to become compatible with limiting global warming to 1.5°C**.
>
> > To achieve this objective, an entity shall disclose:

> Targets set by the entity to mitigate or adapt to climate-related risks or maximise climate-related opportunities, **including an explanation of how these targets are compatible with limiting global warming to 1.5°C.**

4. Transition plans

The inclusion of transition plans within the reporting requirements of entities is welcomed. However, the section lacks reference to a number of essential components, including reference to compatibility with a 1.5°C pathway. Our recommendations are as follows:

Insert the following to paragraph 13(b) (i):

> The processes in place for the review of the targets **and an explanation of their alignment with limiting global warming to 1.5°C.**

Insert a new point (iv) underneath paragraph 13(b):

> **The locked-in GHG emissions from key assets and products, including an explanation if and how these can jeopardise the achievement of GHG emission reduction targets and drive transition risk, and the plans to manage GHG-intensive assets and products.**

Insert new points (c) and (d) under paragraph 13:

> **An explanation of how the transition plan is embedded in and aligned with its overall business strategy and financial planning and whether it is approved by the administrative, management and supervisory bodies of the undertaking.**
>
> **An explanation of how the transition plan is embedded in and aligned with Just Transition principles as defined by the Climate Justice Alliance.[3]**

5. Governance of reporting companies

We have identified two areas in which the requirements concerning the governance of reporting entities could be further enhanced (p.33).

First, it is essential to ensure that the person(s) responsible for managing climate-related risks do not have conflicts of interest that would prevent them from effectively carrying out their duties in this regard, for example by sitting on the board of an oil or gas company.

We therefore suggest inserting a new point after paragraph 5(b):

> **How the entity prevents conflicts of interest from arising within the body responsible for climate-related risks, opportunities, and impacts.**

[3] https://climatejusticealliance.org/wp-content/uploads/2019/11/CJA_JustTransition_highres.pdf

Furthermore, there is presently no mention of the importance of ensuring a just transition, climate justice, or justice, equity, diversity and inclusion in the composition of the governance body or bodies overseeing climate-related management.

We therefore suggest inserting a new point after paragraph 5(c):

> **How the body ensures that diverse and inclusive representation is available to oversee strategies designed to respond to climate-related risks, opportunities, and impacts.**

6. **Strategy & decision-making**

The Exposure Draft should incorporate an additional and explicit requirement for entities to disclose due diligence activites with respect to Indigenous peoples and local communities under the section on carbon offsets and transition plans. Forest- and land-based carbon offset programmes have a well-documented history of enabling and/or exacerbating rights violations of Indigenous and local communities residing in those areas, and the establishment of additional offset programmes could increase conflicts with communities. Moreover, conflict with local communities has in the past threatened the integrity of the carbon offsets themselves, introducing risk to financial entities.

We would therefore recommend inserting a new point under paragraph 13(b) (iii):

> **Clear identification of the project from which the carbon offsets are sourced, along with detailed information on the steps taken to ensure that the rights of Indigenous and local communities residing in the areas where that offset project is operating are protected.**

7. **Metrics & Targets**

We believe that entities should additionally be recommended to use GHG Protocol compliant methodologies, namely the Partnership for Carbon Accounting Financials (PCAF), to disclose so-called "financed emissions."

The PCAF Global GHG Accounting & Reporting Standard for the Financial Industry is the GHG Protocol-endorsed accounting and disclosure methodology for Category 15 of the GHG Protocol Scope 3 inventory. PCAF comprises Scopes 1, 2, and 3 emissions from companies that banks, asset managers, and other financial institutions are investing in or lending to. To date, $US 74 trillion in assets have been committed to the PCAF standard, including small and large financial institutions.

The most recent guidance from the Task Force on Climate-Related Financial Disclosures (TCFD) recommends the use of PCAF for measuring and disclosing financed emissions[4], and it is also referenced in new banking regulations in the European Union.[5]

[4] https://assets.bbhub.io/company/sites/60/2021/07/2021-Metrics_Targets_Guidance-1.pdf
[5] https://www.eba.europa.eu/eba-publishes-binding-standards-pillar-3-disclosures-esg-risks

We suggest that the S2 Climate-related Disclosures introduce a recommendation for financial institutions, especially banks, to disclose financed emissions under PCAF in the first year of reporting, as well as oblige financial institutions to follow the latest versions of the standard within one year after each release, as periodic updates become available. The PCAF standard is expanding to include emissions removals, sovereign bonds, as well as "facilitated" emissions, namely new categories of financed emissions including insured emissions and capital markets.

8. Targets

Finally, we suggest that the Exposure Draft include provisions for what happens if a disclosing entity misses its targets, for example by adding a new bullet under paragraph 23:

> **Actions to be taken if the climate-related target is not reached.**

We welcome that the IFRS and ISSB are seeking advice to inform their work to develop comprehensive climate-related disclosures for market participants. This is a timely intervention and an essential means that enable the valuing of companies for retail and institutional investors.

Yours truly,

Marilyn Waite

Managing Director, Climate Finance Fund