



Consultation on draft IFRS climate-related disclosure standards and accompanying industry-based disclosure requirements for financial institutions

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RMI is an independent non-profit founded in 1982 that transforms global energy systems through market-driven solutions to align with a 1.5°C future and secure a clean, prosperous, zero-carbon future for all. RMI works in the world's most critical geographies and engage businesses, policymakers, communities, and NGOs to identify and scale energy system interventions that will cut greenhouse gas emissions at least 50 percent by 2030. With more than 500 staff, RMI has offices in Basalt and Boulder, Colorado; New York City; Oakland, California; Washington, D.C.; and Beijing.

The consultation response is submitted by the PACTA team under RMI's Climate Finance programme. PACTA (the Paris Agreement Capital Transition Assessment) is one of the leading climate scenario analysis approaches and tools in the world, applied by banks, investors, supervisors, and governments in all major financial markets. PACTA measures a financial portfolio's alignment with climate scenarios by comparing 5-year forward-looking production plans of financed companies in climate critical sectors with required decarbonization efforts prescribed by climate change mitigation scenarios.

PACTA's is both a tool and methodology that are open-source, free of charge, independent and science-based, and actionable. Since its launch, the concept promoted by PACTA has been integrated into the practices of major financial institutions (with more than 1,500 users worldwide), as well as by supervisors and central banks (EIOPA, California Department of Insurance, Bank of England, and more). PACTA has been used by a quarter of the world's 100 largest banks and investors, as well as having been endorsed by the Austrian, Swiss, Norwegian, and Swedish government as part of their market alignment tracking work involving over 400 European financial institutions.

RMI welcomes the proposed standards in many respects as they represent an important step in mainstreaming climate-related scenario analysis and assessment of commercial climate resilience in financial institutions across the globe. This document provides RMI's comments in relation to the climate-related scenario analysis **Question 7** together with the financial industry-related **Question 11** of the online survey, as indicated by the VRF team.

Please do not hesitate to contact Nicholas Dodd (ndodd@rmi.org) for further information on any of the comments made in this response or to find out more about PACTA and the Climate Finance programme at RMI.

Question 7–Climate resilience

Paragraphs BC86–BC95 of the Basis for Conclusions describe the reasoning behind the Exposure Draft’s proposals.

(a) Do you agree that the items listed in paragraph 15(a) reflect what users need to understand about the climate resilience of an entity’s strategy? Why or why not? If not, what do you suggest instead and why?

We **broadly agree**, but a significant missing item is reference to the planned role and contribution that a financial entity will play in the mitigation of climate change and, in the context of scenarios and their sectoral decarbonisation pathways, the need to put in place internal processes to measure the alignment of their portfolios to these pathways and to identify the commercial opportunities related to investment and financing needs of investees and counterparties along pathways. This in turn will need to be associated with processes of engagement and internal decision-making processes – both of which could be highlighted under 15(a)(iii). The importance of engagement and also internal decision-making processes are highlighted by GFANZ’s proposals for FI Transition Plans, which were published for consultation in June 2022.

Whereas scenario analysis informs how a corporate “might” deal with climate change against a set of different hypothetical scenarios – i.e an assessment of its resilience - It does not speak to how it is “dealing with or contributing to climate change”. For this we need a new set of metrics – Climate scenario **alignment** metrics.

The former could reveal a good level of resilience of a corporate based on their diversification activities i.e they may have good hedging systems in place that allow for them to continue being a robust business in light of climate change. But this doesn’t speak to their actions to align with global climate goals and hence mitigate the risks of climate change in the real economy and hence the worst of its effects on the financial system over longer time horizons.

The latter would look at how a corporates activities (real economic activities) align with climate goals. In this case the climate goals are read from scenarios and translated into sectoral pathways that provide one potential route for the given sector to achieve climate goals. This speaks directly to how the corporate is contributing to a given climate goal as opposed to its resilience to deal with a climate impact (shock).

To address climate change and in particular to mitigate the risks of climate change on the financial system an ex ante approach to risk management is required – i.e. one that is forward looking and **pro-active**. So the question should be “what actions/contributions is a corporate taking to address climate change and the inverse mitigate it”. Rather than the reactive – now that it has happened “how good is the company at dealing with it”.

Climate **alignment** metrics are essential for sectors where well-defined climate transitions are recognised as being needed (Fossil Fuel production, Power production, transport, industries such as steel and cement). Climate change needs to be addressed in an ex-ante manor for high emissions sectors – therefore the approach to scenario analysis should incorporate the use of metrics to evaluate resillience that are forward looking and ones that look at the company’s contribution to mitigation aims. The most actionable metrics would be those that measure changes in real economic units of output that are required to change in order to align with a low carbon transition (e.g. building

out renewables at the rate prescribed from the IEA SDS) or the rate it is decreasing (ie.g. reduce the energy coming from coal).

(b) The Exposure Draft proposes that if an entity is unable to perform climate- related scenario analysis, that it can use alternative methods or techniques (for example, qualitative analysis, single-point forecasts, sensitivity analysis and stress tests) instead of scenario analysis to assess the climate resilience of its strategy.

(i) Do you agree with this proposal? Why or why not?

We **broadly disagree**, as FIs should be encouraged to work towards putting in place the resources to make consistent quantified disclosures based on scenario alignment measurements.

(ii) Do you agree with the proposal that an entity that is unable to use climate-related scenario analysis to assess the climate resilience of its strategy be required to disclose the reason why? Why or why not?

We **broadly agree**, as the reasons should be made transparent to external users.

(iii) Alternatively, should all entities be required to undertake climate-related scenario analysis to assess climate resilience? If mandatory application were required, would this affect your response to Question 14(c) and if so, why?

We **broadly agree**, as per our response to 2(b)(i), and if this were to be the case the effective date should allow for an implementation period.

(c) Do you agree with the proposed disclosures about an entity' s climate-related scenario analysis? Why or why not?

Other – at a general level the way in which the scenario will be used to assess climate resilience is currently not referred to. Scenario alignment measurement is recognised by the TCFD and the wider industry as the main quantified form of scenario analysis, and in our view should be the focus for this standard. From a scenario alignment perspective the following key items are missing from the general framework of the disclosure:

- Decarbonisation pathways: Reference is needed not just at a high level to scenarios but also to their component sectoral decarbonisation pathways. These pathways are required in order to make sectoral or activity level alignment measurements.
- Allocation methods: In the case that scenario alignment measurements are made the methodology for allocating the required macro-level changes in GHG emissions, technologies or production prescribed by the scenario to micro-economic actors should be specified. Examples can be found in the PACTA methodology and also in Appendix D of ISO 14097.
- Forward looking alignment measurement metrics: Reference is needed to how scenarios will be used to provide quantifiable measurements of the alignment of investees and counterparties with scenarios. This should include specific reference to the use of alignment metrics to measure progress along decarbonisation pathways.
- Portfolio and client-level data: For applications of scenario analysis by financial institutions covered by the proposed requirements of Volumes B15-18, reference is needed to the source and data quality of client level data on GHG emissions and production.

These items could potentially be specified as a methodological components of the Volume B15-18 disclosure requirements, as part of ensuring that they include the use of scenario alignment metrics (see our response to Q11.k).

(d) Do you agree with the proposed disclosure about alternative techniques (for example, qualitative analysis, single-point forecasts, sensitivity analysis and stress tests) used for the assessment of the climate resilience of an entity’ s strategy? Why or why not?

We **broadly disagree**, as FIs should be encouraged to work towards putting in place the resources to make consistent quantified disclosures based on scenario alignment measurements. Stress tests, for example, require similar datasets to scenario alignment measurement,

(e) Do the proposed disclosure requirements appropriately balance the costs of applying the requirements with the benefits of information on an entity’ s strategic resilience to climate change? Why or why not? If not, what do you recommend and why?

We broadly agree as the opportunity costs are relatively low given that climate change is creating an increasing commercial driver for FIs to obtain information on their strategic resilience. We do not consider that the data acquisition and entry level costs of access and training to prepare such disclosures are significant when put in the context of other data overheads, including ESG data.

RMI is steward of the PACTA climate scenario analysis methodology and tool. PACTA has been developed in a way that aims to reduce the entry level costs and barriers for FIs wishing to carry out climate scenario alignment measurements for climate critical sectors. It provides the means for both investors and banks to carry out analysis of equity, bond and loan portfolios.

The second set of proposed changes relative to existing SASB Standards address emerging consensus on the measurement and disclosure of **financed or facilitated emissions in the financial sector**. To address this, the Exposure Draft proposes adding disclosure topics and associated metrics in four industries: commercial banks, investment banks, insurance and asset management. The proposed requirements relate to the lending, underwriting and/or investment activities that finance or facilitate emissions. The proposal builds on the GHG Protocol Corporate Value Chain (Scope 3) Standard which includes guidance on calculating indirect emissions resulting from Category 15 (investments).

Paragraphs BC149–BC172 of the Basis for Conclusions describe the reasoning behind the Exposure Draft’s proposals for financed or facilitated emissions.

11(d) Do you agree with the proposed industry-based disclosure requirements for financed and facilitated emissions, or would the cross-industry requirement to disclose Scope 3 emissions (which includes Category 15: Investments) facilitate adequate disclosure? Why or why not?

Please select which industries you would like to comment on. If you would like to comment on all industries select 'All industries'.

- All industries
- Asset Management & Custody Activities
- Commercial Banks
- Insurance
- Investment Banking & Brokerage

Our comments will be of relevance for all four of the types of financial institution targeted by the industry-based disclosure requirements. We **agree** that the proposed industry-based disclosure

requirements for these four types of institution are required. This is because the attribution of CO₂ emissions to portfolios, whether they be securities or loans, requires specific methodologies and rules.

(e) Do you agree with the industries classified as 'carbon-related' in the proposals for commercial banks and insurance entities? Why or why not? Are there other industries you would include in this classification? If so, why?

Broadly Agree

Broadly Disagree

Other

Please explain your answer:

We **broadly agree** with the classification of 'carbon-related' industries. This is because they include amongst them the highest CO₂ emitting activities. The same classification should be used across the four types of financial institutions for which standards are proposed to be established.

For the purpose of pinpointing those points in the value chain of different economic activities at which financial institutions can exert the greatest direct influence via decision-making and engagement, we would recommend defining more precisely those economic activities within scope by using NACE or SIC codes. For example, upstream oil & gas production, steel and cement production, vehicle manufacturing.

(f) Do you agree with the proposed requirement to disclose both absolute- and intensity-based financed emissions? Why or why not?

Broadly Agree

Broadly Disagree

Other

Please explain your answer.

We **broadly disagree** with the proposed requirement. The stated use case for the disclosures is external users, so whilst absolute CO₂ emissions for critical sectors such as power generation, fossil fuel production and automotive production, can have a value in communicating relative exposure and adaptive capacity, there are other production-based metrics that in our view can provide a clearer basis for measuring the alignment of portfolios with climate-related scenarios and a clearer link to actionability in the short term. In relation to intensity-based emissions metrics, in our view physical intensity metrics normalised to units of production should be specified instead of financed intensity metrics, which are technically flawed in that they:

1. do not provide a unit of measurement with which progress can be readily measured against climate-related scenarios, and
2. provide results that are susceptible to volatility in the market value of securities, which is particularly an issue for asset managers and insurance companies.

In the case of the latter point, the GHG protocol recognises this issue and provides some guidance (see p-51), which should be referred to in the disclosure standard:

'Because investment portfolios are dynamic and can change frequently throughout the reporting year, companies should identify investments by choosing a fixed point in time, such as December 31 of the reporting year, or using a representative average over the course of the reporting year.'

We also note that physical intensity metrics are widely used in climate related scenarios, such as those developed by the IEA and the European Commission, as well as in financial sector and industry disclosures. They can therefore readily be used as a technology neutral metric for measuring climate-related scenario alignment at both counterparty and portfolio level.

One concern with absolute portfolio level emissions is that this can be easily improved by portfolio re allocation into low carbon sectors. Whereas this may align the portfolio to a given target which may be useful from a risk perspective it should not be convoluted to suggest this portfolio has created "impact" in the real economy. By requesting this metric, our fear is that it could incentivise such behaviour and

that the underlying assets would be re distributed to financial institutions that are not adhering to these disclosure requirements. Our suggestion would be to use sectoral disclosures and to re baseline when the portfolio changes.

(g) Do you agree with the proposals to require disclosure of the methodology used to calculate financed emissions? If not, what would you suggest and why?

Broadly Agree

Broadly Disagree

Other

Please explain your answer:

We **broadly agree** with the proposal to require disclosure of the methodology used to calculate 'financed' emissions. Transparency on methodological choices is essential in order to build confidence amongst end users of disclosures, including at supervisory level, as well as to encourage an ongoing debate on the effectiveness and impactfulness of different metrics. This should extend to methodological choices that are currently left open ended in the industry-specific guidance, such as the exact methods for attributing emissions from the corporates to the portfolio level e.g. equity ownership, enterprise value, portfolio weight.

(h) Do you agree that an entity be required to use the GHG Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard to provide the proposed disclosures on financed emissions without the ISSB prescribing a more specific methodology (such as that of the Partnership for Carbon Accounting Financials (PCAF) Global GHG Accounting & Reporting Standard for the Financial Industry)? If you don't agree, what methodology would you suggest and why?

Broadly Agree

Broadly Disagree

Other

Please explain your answer:

We **broadly disagree** with this position. There are three main reasons for this view:

1. The concerns we cited in relation to financed emissions intensity metrics in Q11.f highlight the need to refer to a standard such as PCAF in order to reference alternative metrics, as well as other methodologies that are specific for the financial sector and which may require specification to ensure consistent reporting, such as in the case of:
 - a. portfolio attribution of loans and securities,
 - b. how to treat corporate lending facilities based on their status,
 - c. how to attribute climate units of measurement to facilitated services such as underwriting.

Facilitated services is a relatively new area of methodological development in which PCAF has recently focused on standards development for underwriting and securities issuance.

2. As we have already highlighted, we consider that there are other metrics, such those based on capacity which are used within the PACTA methodology, that can be effective and which can also benefit from reference to a common standard, such as ISO 14097 Annex D: Guidance on outcome and emissions trajectory quantification, where the three main types of PACTA climate scenario alignment metrics can be located.
3. Using the production-based metrics referred to in the second point could avoid the complexities of defining and attributing scope 3 based emissions to an entity. In this respect the GHG protocol is open ended and doesn't address the issues related to, for example:
 - a. the definition of scope 3 emissions for automotive manufacturers when the use phase emissions can only be estimated on an emissions intensity basis from test results, or
 - b. the need for allocation rules to avoid the double counting of emissions between sectors in a portfolio, as in the case of oil production and automotive production.

(i) In the proposal for entities in the asset management and custody activities industry, does the disclosure of financed emissions associated with total assets under management provide useful information for the assessment of the entity's indirect transition risk exposure? Why or why not?

Broadly Agree

Broadly Disagree

Other

Please explain your answer:

We **broadly disagree** with the statement. In terms of the proposed metric, we do not consider financed emissions to be a suitable metric for assessing transition risk exposure. This is because they do not measure the relative exposures across different high emitting sectors or allow for measurement of climate-related scenario alignment as an indicator of transition risk. The denominator of assets under management is a relevant unit for measuring financial exposure.

Overall, the proposed industry-based approach acknowledges that climate-related risks and opportunities tend to manifest differently in relation to an entity’s business model, the underlying economic activities in which it is engaged and the natural resources upon which its business depends or which its activities affect. This affects the assessment of enterprise value. The Exposure Draft thus incorporates industry-based requirements derived from the SASB Standards.

The SASB Standards were developed by an independent standard-setting board through a rigorous and open due process over nearly 10 years with the aim of enabling entities to communicate sustainability information relevant to assessments of enterprise value to investors in a cost-effective manner. The outcomes of that process identify and define the sustainability-related risks and opportunities (disclosure topics) most likely to have a significant effect on the enterprise value of an entity in a given industry. Further, they set out standardised measures to help investors assess an entity’s performance on the topic.

Paragraphs BC123–BC129 of the Basis for Conclusions describe the reasoning behind the Exposure Draft’s proposals related to the industry-based disclosure requirements.

While the industry-based requirements in Appendix B are an integral part of the Exposure Draft, forming part of its requirements, it is noted that the requirements can also inform the fulfilment of other requirements in the Exposure Draft, such as the identification of significant climate-related risks and opportunities (see paragraphs BC49–BC52).

(j) Do you agree with the proposed industry-based requirements? Why or why not? If not, what do you suggest and why?

Broadly Agree
Broadly Disagree
Other

Please explain your answer:

Other - whilst we agree with the need for industry-based requirements for this specific sector, for previously cited reasons we consider that the currently proposed metrics are not all suitable, in particular finance emissions intensity and that, moreover, the scope and time horizon of the metrics should complement the focus on the importance of climate-related scenario analysis in the Climate Related Disclosures draft (see our response to 11.k below).

(k) Are there any additional industry-based requirements that address climate-related risks and opportunities that are necessary to enable users of general purpose financial reporting to assess enterprise value (or are some proposed that are not)? If so, please describe those disclosures and explain why they are or are not necessary.

Yes

No

Other

Please explain your answer:

The disclosure metrics should complement the importance given to climate-related scenario analysis in the Climate Related Disclosures draft. In this respect the measurement of alignment with scenario decarbonisation pathways should be a key disclosure objective, with measurement using units of emissions, emissions intensity and production being options.

This type of measurement, when made on a short term time horizon of 5-10 years, can provide critical information to assess the climate resilience of an entity (as referred to on p-37) and the future potential for commercial value creation (or destruction), including:

- the likely real economy impact of planned investments by investees and counterparties, as well as sectoral needs for investment and financing in order to meet scenario targets.
- a strategic outlook at a portfolio level as to how the business model may have to be adjusted in order to request, support and enable climate change mitigation actions by investees and counterparties.

The use of forward-looking portfolio alignment metrics was recommended by the TCFD in their guidance of October 2021 and is the subject of further methodological development work by GFANZ in the run up to COP27. Even accepting the challenges of adoption of scenario analysis by the sector, a place marker should be included in each of Volumes B15-18, giving the option for reporting for those financial institutions that have begun using scenarios as a tool.

(I) In noting that the industry classifications are used to establish the applicability of the industry-based disclosure requirements, do you have any comments or suggestions on the industry descriptions that define the activities to which the requirements will apply? Why or why not? If not, what do you suggest and why?

Yes

No

Other

Please explain your answer:

Yes – whilst we agree with the general focus of the four volumes B15-18 on banking, investment and insurance entities, the focus on the facilitated emissions of ‘pure play’ banks in B18 should be expanded to also be included within volume B16, as these entities may have both corporate and investment banking divisions.