Investor Group on Climate Change

Investor Group on Climate Change (IGCC)

Submission to:

External Reporting Board's *Aotearoa New Zealand Climate Standard 1: Governance and Risk Management Consultation Document*

November 2021

Tom Arup
tom.arup@igcc.org.au
www.igcc.org.au

About IGCC

The Investor Group on Climate Change (IGCC) is a collaboration of Australian and New Zealand investors focused on the impact that climate change has on investment. IGCC represents institutional investors with total funds under management of over AUD$2 trillion in Australian and New Zealand and over AUD$20 trillion globally, and others in the investment community interested in the impact of climate change. IGCC members cover over 7.5 million people in Australia and New Zealand.

Overview

IGCC welcomes the opportunity to make a submission on the External Reporting Board (XRB) *Aotearoa New Zealand Climate Standard 1 (NZ CS 1): Governance and Risk Management Consultation Document* (Consultation Document).

A mandatory climate risk disclosure regime in New Zealand is a welcome development that is supported by investors. Over time it will improve the quality of information needed to manage climate risk. It is hoped it will also efficiently support the allocation of capital to a net zero greenhouse gas (GHG) emissions economy.

IGCC believes New Zealand's standards for climate risk disclosure should be built on the following principles. They should:

- Be compatible and comparable to the standards being set globally, both through international baselines like those being developed by the International Sustainability Standards Board, and with the activity of major markets in Europe, Asia and North America who are expanding beyond these minimum standards.
- Be subject to an iterative review process to allow a build-up of practice by reporting entities over time and ensure standards reflect rapidly shifting policy, practice and science to ensure the New Zealand economy remains competitive in capital markets.
- Encourage better practice, not just in the minimum expectations of standards themselves but through the information provided in guidance.

Developing clear standards for reporting will be critical to the New Zealand disclosure regime's success, including whether it will drive the market critical information needed by primary users like investors. The External Reporting Board (XRB) to date has been highly constructive, inclusive of investor needs and focused on the importance of driving strong disclosure. It is clear in many aspects of the Consultation Document that the XRB is seeking to ensure the standards for the disclosure regime (Standards) will help New Zealand achieve the aims of mandatory climate reporting and the needs of primary users.

Some aspects outlined in the Consultation Document require further development, such as strengthening reporting requirements on board skills in the Governance section.

IGCC recommendations on the specific questions asked by the XRB at this stage of the consultation are summarised in Table 1 below.

Table 1. IGCC recommendations on Aotearoa New Zealand Climate Standard 1: Government and Risk Management Consultation Document

XRB Questions	IGCC Recommendation
Primary users have been identified as existing and potential investors, lenders, and insurance underwriters. Do you think that all these users should be included in the primary user category?	• Maintain proposed listed primary users and definitions • Consider adding “policymakers and financial regulators”
Do you think the proposed Governance section of NZ CS 1 meets primary user needs? **a. Do you think that the information provided under this section of NZ CS 1 will provide information that is useful for decision making to primary users (existing and potential investors, lenders and insurance underwriters)? If not, please explain why not and identify any alternative proposals.** **b. Do you consider that this section of the standard is clear and unambiguous in terms of the information to be disclosed? If not, how could clarity be improved?** **c. Do you consider that this section of the standard is adequately comprehensive and achieves the right balance in terms of prescriptiveness and specificity? If not, what should be removed or added to achieve a better balance?**	• The reporting entity should be required to disclose its identified and current board skills by publishing a matrix, with climate change being a skill that directors are assessed against if deemed material. • Define ‘climate change skills’ as it relates to boards and management in the Standards and use guidance to address the perceived risk of adding a disclosure on specific board skills and competencies might inadvertently create an expectation that all boards should have specific climate expertise resulting in a ‘shopping list’ for directors’ expertise. • If the XRB does not believe the Standards should require publication of a full board skills matrix, then reporting entities should be asked to identify whether climate change is a skill needed as part of the mix of skills the board requires to oversee the organisation. If so, the reporting entity should state those director/s it believes have these skills, and if none, how it intends to bring these skills onto the board (through appointments, training or standing external expertise). If climate change is not deemed a relevant board skill the entity should then disclose why. • Add “and how they are assessed” to the end of the clause at 4(c) • Add “strategy” to the clause at 4(e) where it states, “governance and decision making” • Align clause 5(c) with 4(a) by adding “frequency” in 5(c) • Consider adding governance metrics such as the frequency of meetings and workshops on climate

	change, proportion of time or number of board meetings allocated to the issue, renumeration, performance and financial incentives. This could also be encouraged in guidance.
Do you think the proposed Risk Management section of NZ CS 1 meets primary user needs? **a. Do you think that the information provided under this section of NZ CS 1 will provide information that is useful for decision making to primary users (existing and potential investors, lenders and insurance underwriters)? If not, please explain why not and identify any alternative proposals.** **b. Do you consider that this section of the standard is clear and unambiguous in terms of the information to be disclosed? If not, how could clarity be improved?** **c. Do you consider that this section of the standard is adequately comprehensive and achieves the right balance in terms of prescriptiveness and specificity? If not, what should be removed or added to achieve a better balance?**	• Consider adding a requirement to report the types of climate-related risks that were assessed by the reporting entity alongside the process for identifying the risks. This would be separate to setting out the identified material risks for a reporting entity in reporting against the strategy section. • Consider whether Section 5 could be more explicit in asking for disclosure on how a reporting entity *prioritises* different risks.
The XRB has primarily drawn from the TCFD's definitions for its defined terms. Do you agree that we should align closely with the TCFD's definitions? **The XRB is particularly interested in feedback on the following defined terms as they are currently proposed: 'climate-related risk,' 'climate-related opportunities,' 'climate-related**	• Maintain current definitions • Establish a definition for "climate change skills" as it relates to boards and management based on the *World Economic Forum Climate Governance Principles*, *Changing Climate*, Cluster 4 of the European Financial Reporting Advisory Group's sustainability reporting standards roadmap, and other relevant sources.

issues,' 'physical risk,' and 'transition risk.' **a. Do you consider that the XRB should align with the TCFD and use the terms 'climate-related opportunities' and 'climate-related issues', or should we only refer to 'climate-related risks'?** **b. Do you consider that the proposed definitions for these terms are accurate, sufficiently clear and well-explained? Do they need further detail or explanation? If so, should that detail be included in the defined terms or in guidance?** **Do you have any other views on the defined terms as they are currently proposed?**	
The XRB is currently of the view that adoption provisions for some of the specific disclosures in NZ CS 1 will be required. However, the XRB does not believe it is necessary to provide any adoption provisions for entities in relation to the Governance and Risk Management disclosures. Do you agree with this view? Why or why not?	• Maintain proposed approach
The XRB currently intends NZ CS 1 to be concise and sector neutral, with sector specific requirements to be contained in guidance. Do you agree with this approach?	• Maintain proposed approach
Do you have any other comments?	• Set out a timeline for expected reviews and updates of the Standards and associated guidance. • Consider further specific guidance for the voluntary use of the Standards by unlisted companies and other uncovered entities. • Consider how to explicitly align the Standards and guidance to the objectives of the Climate Change Response Act.

Introduction

IGCC has been supportive of the development and implementation of the mandatory climate risk disclosure regime in New Zealand.[1] Voluntary disclosures based on the 2017 recommendations of the Task Force for Climate-related Financial Disclosure (TCFD) have driven a major step forward across many markets in the practice and volume of climate-related reporting. However, many critical issues remain in terms of the quality and coverage of reporting. This has meant overall reporting has been insufficient for the needs of investors, and other primary users to assess companies, mitigate climate risk and efficiently allocate capital towards the net zero transition.

In response several jurisdictions are implementing disclosure requirements that are either wholly mandatory or have mandatory aspects. New Zealand is by no means alone in this regard. These mandatory regimes are broadly predicated on delivering:

- Comparable and consistent reporting across markets for end users and usages
- Clear information to help assess climate risk and opportunity exposure at the entity, market and economy-wide level
- Clear expectations, guidance and standards for regulated entities as a basis for their reporting

The New Zealand mandatory regime is well positioned to deliver on the above, with robust and globally consistent standards for reporting underpinning it.

The XRB to date has been highly constructive, inclusive of investor needs and focused on the importance of driving strong disclosure. Many aspects of the Consultation Document indicate that the XRB is seeking to ensure the Standards will help New Zealand achieve the aims of mandatory climate reporting and the needs of primary users.

It is worth noting that without linking climate risk disclosure standards back to an actual objective or target, reporting is at risk of becoming a box ticking exercise. IGCC therefore recommends aligning the Standards and/or guidance with and purpose, objectives and targets of the Climate Change Response Act, as amended by the Climate Change Response (Zero Carbon) Amendment Act 2019***.***

Some specific aspects outlined in the Consultation Document also require further development, including strengthening reporting requirements on board skills in the Governance section.

Investor needs

The *Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill* (the Bill) rightly identifies one of the purposes of mandatory disclosure in New Zealand as to “enable investors and other stakeholders to assess the merits of how entities are considering those risks and opportunities.”[2]

Institutional investors understand that climate change is one of the most significant investment risks and opportunities facing the industry today. The economic impacts of climate change present material risks to

[1] https://igcc.org.au/wp-content/uploads/2020/06/IGCC-submission-NZ-Climate-Disclosures-Dec19-FINAL.pdf
[2] https://legislation.govt.nz/bill/government/2021/0030/latest/whole.html#LMS479633

the investment returns of long-term asset owners and their beneficiaries. The scale of these risks is systemic, and investors are deploying a range of management strategies to mitigate this risk and better maximise opportunities. These strategies include company engagement and strategic capital allocation. Credible climate risk reporting by companies is critical for both.

Investors in New Zealand and internationally support the phase in of mandatory economy-wide TCFD-aligned disclosures.[3][4] This broad industry support for mandated disclosures recognises that the ongoing absence of adequate information on climate risk and opportunities is already contributing to systemic financial stability risks and barriers to investment in zero emissions and climate resilient economic activity.

Investor experience with voluntary disclosure has been mixed. The 2020 IGCC report – *Full disclosure: improving corporate reporting on climate risk* (*Full Disclosure*) – canvassed the views of 22 Australian and New Zealand investors responsible for a combined NZD$1.14 trillion in assets under management, on their experience and expectations of corporate disclosure.[5]

That report found that investors expect companies to:

- Demonstrate board, director and executive skills and expertise in climate change
- Report links between climate-related performance and executive remuneration
- Demonstrate links between risks and opportunities identified and the company's strategic and organisational response
- Extend reporting of GHG emissions metrics and targets to Scope 3 emissions
- Report on both transition and physical risks, costs and implications
- Provide auditing and assurance of results as it becomes more important

Critically, investors want companies to show not just that climate risk is being assessed but how this is informing and changing their strategies and decision making from board governance to capital expenditure to future business opportunities.

Globally, disclosure by investors have somewhat lagged the volume that has emerged from listed companies or other sectors.[6] This is in part reflecting the initial focus of the TCFD on listed corporates, as well as owing to the complexity of the metrics and frameworks required to make full portfolio assessments of risks and opportunities, and the necessity of better data from the disclosure companies to aid this.

These elements require standard setters and regulators to recognise the reporting quality from investors will in part be determined by company reporting standards and other data availability overtime. However, there is growing recognition that the lack of data should not serve as an excuse for investors[7] and the volume of investor disclosure has grown globally in recent years.

[3] https://theinvestoragenda.org/wp-content/uploads/2021/05/IN-CONFIDENCE_EMBARGOED_2021-Global-Investor-Statement-to-Governments-on-the-Climate-Crisis-1.pdf
[4] https://papers.ssrn.com/sol3/Papers.cfm?abstract_id=3437178
[5] https://igcc.org.au/wp-content/uploads/2020/09/IGCCReport_Full-Disclosure_FINAL.pdf
[6] https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/assurance/ey-if-the-climate-disclosures-are-improving-why-isnt-decarbonization-accerlerating.pdf
[7] https://pages.marketintelligence.spglobal.com/rs/565-BDO-100/images/Research-LeadershipInsightsSeries-ClimateChangeAU-211021.pdf?mkt_tok=NTY1LUJETy0xMDAAAAGAQdXc3-w25AIJZ5q-MtuWQYP7zjecKTlzzW3pnbdGetd9L6y9lRE0SAFBYdjH-merFqXWsZ0f2Q6h3D_U0FfN

The Consultation Document also expresses a critical view that mustn't be lost by any reporting entity, including investors, that:

Climate-related disclosures are not intended to be a compliance exercise. Embedding consideration of climate-related issues into an entity's strategy allows for better decision making. This results in more informed capital allocation decisions, both within an entity and by investors into an entity. (p.6)

In short, the proper assessment, mitigation and disclosure of climate-related issues makes for better investors and better investment.

Overarching principles

This submission is structured via the specific questions set out by the XRB in the Consultation Document. However, disclosure standards should be built on the following guiding principles, and it is recommended the XRB continues to consider these issues as it consults on the Governance and Risk Management sections of the Standards, the overall structure of the Standards, and as it develops other sections and guidance.

Globally consistent

To minimise the burden for reporting entities and maximise the value of disclosure, the TCFD stated in its 2020 Status Report that "going forward, it will be important to bring more standardization to reporting requirements across different countries and jurisdictions."[8]

In November 2021, a significant step was taken with the newly established International Sustainability Standards Board (ISSB)[9] and the release of a recommended Prototype Climate-related Disclosures Requirements (Climate Prototype) by the International Financial Reporting Standards (IFRS) Foundation's Technical Readiness Working Group.[10] IGCC welcomed both the establishment of the ISSB and the release of the Climate Prototype, and noted many jurisdictions are already extending beyond these minimum baselines.[11] Standardisation of sustainability reporting standards is an important lever to minimise greenwashing concerns.

Global standards like the Climate Prototype are explicitly intended to create a common baseline for comparability across jurisdictions and these international requirements should be reflected in domestic approaches to aid this cause. At the same time, universal standards should not be the only source standard setters consider. Importantly, the Financial Stability Board and IFRS foundation recognise that sustainability disclosure requirements in many jurisdictions will go beyond the IFRS sustainability requirements and that this is appropriate and encouraged. An example of this is requiring double materiality reporting, i.e., of both impacts of environmental risks and opportunities on the reporting entity, as well as the reporting entity's impacts on the environment and society. New Zealand should aspire for stronger reporting aligned with its global peers who are moving ahead of minimum baselines. Therefore, the developments in markets like the European Union, United Kingdom, United States, Canada, Japan, Singapore, Hong Kong and Australia should also be considered and where relevant matched and even exceeded.

---

8 https://www.fsb.org/wp-content/uploads/P291020-1.pdf
9 https://www.valuereportingfoundation.org/news/ifrs-foundation-announcement/
10 https://www.ifrs.org/content/dam/ifrs/groups/trwg/trwg-climate-related-disclosures-prototype.pdf
11 https://igcc.org.au/investors-welcome-new-international-standards-board-to-deliver-global-climate-disclosure-standard/

IGCC has commissioned consultants Te Whakahaere to conduct a global review of disclosure regimes to determine where common landing areas on different themes are emerging, where there is divergence, and how this might be relevant to the development of the Standards. This research should be available to the XRB and others in late-December to assist in framing all parts of the Standards, and in particular the Strategy and Targets and Metrics sections to come. The findings of this work and other international developments may further shape IGCC's views and recommendations on the Governance and Risk Management sections of the Standards in later consultations.

IGCC supports the XRB's intention to review baseline-level alignment with IFRS sustainability standards under development in the process of developing the draft and final Standards.

Iterative review

Practice and standards have advanced rapidly in just the brief time since the final TCFD recommendations were released in 2017. This includes the guidance being issued by the TCFD itself, which has evolved from high-level principles to much more specific guidance and a toughening of suggested disclosure requirements. A good example of this is the recently finalised TCFD guidance on metrics, targets and transition plans, which marks a significant step up in what could be considered minimum expectations.[12] This evolution towards more specific and prescriptive reporting guidance is a result of the gaps that have been evident in voluntary disclosure, particularly by companies. Further practice and regulation will likely again result in a relatively quick shift in what is considered minimum standards for reporting in coming years.

Disclosure practice will also evolve as the availability of data and granularity of climate models improve. In fact, disclosure can be self-fulfilling, in that the disclosure of some actors like financial organisations is partly dependent on data from other entities like companies. As the disclosure of the latter improves, over time so will the former, again lifting what is possible and considered standard practice. Further innovation, progress and developments in methodologies, data, scenario use, legal opinions, model construction and observed physical climate response may also drive this.

Given this, reporting standards and guidance should not remain static and must both allow for and drive an increase in quality of reporting over time. Outlining clear review timelines and established responsibilities for maintenance of the regime from the outset would help to minimise potential disruption caused by the need to update the Standards. Ultimately, reporting entities should also be preparing for the expectations on reporting to increase over time, not diminish.

Driving better practice

There will always be a tension between usability of disclosure regimes and driving the market critical information required to help primary users manage climate risk. Indeed, this was explicitly referenced in the 2017 final TCFD recommendations which stated: "The Task Force's recommendations aim to be ambitious, but also practical for near-term adoption." But the TCFD also recognised its role in improving reporting over time and that it expected: "to advance the quality of mainstream financial disclosures related to the potential effects of climate change on organizations today and in the future and to increase investor engagement with boards and senior management on climate-related issues."[13]

While the Standards can be considered a floor for reporting under the New Zealand regime, the associated *Climate Standard 2: Adoption of Climate-related Disclosures* (NZ CS 2), guidance and adoption provisions can

[12] https://assets.bbhub.io/company/sites/60/2021/07/2021-Metrics_Targets_Guidance-1.pdf
[13] https://assets.bbhub.io/company/sites/60/2020/10/FINAL-2017-TCFD-Report-11052018.pdf

provide further information not just on what meeting that floor requires but also descriptions of what better and best practice might involve. This would also allow the market to prepare for any future step changes in the Standards or guidance in following years.

Response to Consultation Document questions

1) Primary users have been identified as existing and potential investors, lenders, and insurance underwriters. Do you think that all these users should be included in the primary user category?

IGCC supports the inclusion of the three listed primary users in the Consultation Document and notes its relationship to the TCFD "primary user" definition. We also support the addition of "existing and potential" to the descriptor.

IGCC notes that among the Bill's purpose is that it will: "lead to smarter, more efficient allocation of capital, and help smooth the transition to a more sustainable, low-emissions economy."[14] For New Zealand, a "more sustainable, low-emissions economy" is defined in the *Climate Change Response Act 2002* (The Act), which has been enhanced by the *Climate Change Response (Zero Carbon) Amendment Act 2019*. This includes reaching net zero emissions by 2050 for all greenhouse gases except biogenic methane, reducing emissions of biogenic methane to 24–47 per cent below 2017 levels by 2050, and meeting the established carbon budgets.

In 2020, the Financial Stability Board stated on TCFD disclosure that: "promoting globally consistent, comparable, and reliable climate-related disclosures would help improve the quality of risk monitoring and effectiveness of supervision by financial authorities."[15] IGCC also stated in its 2019 submission on the proposed New Zealand mandatory disclosure regime that: "managing systemic risks to New Zealand's financial system should be central to government and financial regulator actions on climate-related disclosures."[16]

In this light, climate risk disclosure can also provide essential information for policymakers and regulators who are responsible for emissions reductions, economic transition and financial stability. This role is beyond compliance monitoring of disclosure and goes to using the information provided towards understanding and mitigating systemic risks to New Zealand's economy and helping meet the goals of The Act.

Overtime policy makers and regulators may therefore be added to the list of primary users of TCFD disclosure as the financial costs of climate change become larger and more evident. This is something the XRB should monitor in conjunction with global practice and consider as the Standards are developed and updated.

Recommendations:

- **Maintain proposed listed users and definition**

---

[14] https://www.legislation.govt.nz/bill/government/2021/0030/15.0/d13878394e2.html?search=sw_096be8ed81aa816f_leads+to+smarter%2c+more+efficient+allocation+of+capital%2c+and+help+smooth+the+transition+to+a+more+sustainable%2c+low-emissions+economy_25_se&p=1&sr=0

[15] https://www.fsb.org/wp-content/uploads/P070721-4.pdf

[16] https://igcc.org.au/wp-content/uploads/2020/06/IGCC-submission-NZ-Climate-Disclosures-Dec19-FINAL.pdf

- **Consider adding "policymakers and financial regulators"**

2) Do you think the proposed Governance section of NZ CS 1 meets primary user needs?

a) Do you think that the information provided under this section of NZ CS 1 will provide information that is useful for decision making to primary users (existing and potential investors, lenders and insurance underwriters)? If not, please explain why not and identify any alternative proposals.

b) Do you consider that this section of the standard is clear and unambiguous in terms of the information to be disclosed? If not, how could clarity be improved?

c) Do you consider that this section of the standard is adequately comprehensive and achieves the right balance in terms of prescriptiveness and specificity? If not, what should be removed or added to achieve a better balance?

IGCC agrees with many aspects of the proposed Governance section of the Standards.

IGCC is supportive of the demarcation of reporting requirements for both the role of the board and management in addressing climate-related issues, reflecting the different governance roles they play in and for an organisation. However, to ensure consistency between the disclosure requirements for management and board activity, "frequency" should be added to the clause at 5(c) to align it with clause 4(a).

The inclusion and elevation of remuneration policies to the Governance section is also important and reflects to a degree Climate Prototype clause 4(f). Although this could be strengthened by adding "and how they are assessed" to the end of clause 4(c) of the Standards to drive disclosure on how these metrics are being assured and tracked so that primary users can further assess their robustness.

There is good specificity in terms of asking for information about the processes boards and management are taking in relation to climate change, and this should be carried through to the final version of the Standards. In particular, the inclusion of clause 4(e) as it addresses the concerns of investors noted in *Full Disclosure* about the lack of connection between climate disclosure and broader strategy, although "strategy" should be included alongside "governance processes and decision making" in this clause.

The specificity of the processes that is required to be disclosed by the standards could be enhanced by adding metrics to Governance section. This could include requiring the reporting on the frequency of meetings and workshops on climate change; the proportion of time or the number of meetings allocated to the issue at the board or board committee level; renumeration; performance; and financial incentives. For example, in 2020 Barclays reported on the proportion of time its Board Risk Committee committed to specific areas.[17] These metrics could also alternatively be encouraged through guidance.

The framing of parts of the board reporting requirements are too limited because of the underlying assumption in the Consultation Document that: "The risk with adding a disclosure on specific board skills and competencies is the inadvertent creation of an expectation that all boards should have specific climate expertise resulting in a 'shopping list' for directors' expertise." As a result, the balance of the proposed Standards is tilted away from what IGCC believes are reasonable requirements on reporting entities

[17] https://home.barclays/content/dam/home-barclays/documents/investor-relations/reports-and-events/annual-reports/2020/Barclays-PLC-Annual-Report-2020.pdf

to disclosure how climate change skills are viewed as part of an overall mix of board skills needed and which directors hold said skills. The XRB's concerns about potential inadvertent expectations could be addressed through guidance, rather than limiting the Standards.

This current position in the Standards generally does not reflect the needs identified by investors as primary users of disclosure.[18] Investors rely on the companies they invest in to manage climate change risk. Shareholders elect directors and rely on boards to set strategy and oversee risk management. Coupled with the fiduciary duty to manage climate risk across portfolios, this means investors need information to make clear assessments about whether the skills on a board as it relates to climate change is appropriate and whether that reflects a risk to investment.

The implications of having boards that are not "climate competent" can be profound and present a material risk to the returns that investors are required to deliver to their beneficiaries. The recent IGCC report – *A changing climate: What investors expect of company directors on climate risk* (*Changing Climate*) – details the potential material implications of a board that is not climate competent such as misjudging technology development leading to stranded assets or asset write downs.[19]

Changing Climate also sets out investor expectations for directors and boards on climate change including the reporting of board responsibilities and skills, and what should be considered a "climate competent" board. See Table 2 below for relevant expectations to the Standards, and the final *Changing Climate* report for the full list of investor expectations.

Table 2. Relevant investor expectations in Changing Climate on board skills disclosure

Topic	Investor Expectations
Board structure and committees	• Board committees should disclose the significant climate change-related issues that they have considered and the outcomes of these considerations
Board skills matrix	• Report on how the skills matrix is developed and the process of assessing director skills on climate-related issues • Independent assessment, or audit, of company director skills • A brief description of the criteria the board uses to assess each skill or background in the skills matrix • Differentiation between directors with significant expertise or experience of a particular skill, versus knowledge or awareness in a particular area. This applies not only to climate change-related skills, but all skills identified in the board skills matrix

[18] https://igcc.org.au/wp-content/uploads/2020/09/IGCCReport_Full-Disclosure_FINAL.pdf
[19] https://igcc.org.au/wp-content/uploads/2021/11/IGCC-Climate-Change-Board-Report.pdf

	• Disclosure of a board succession plan outlining how necessary climate change-related skills will be brought onto the board
Director competency and backgrounds	• Disclosure of relevant experience and expertise: Details of director backgrounds need to demonstrate the expertise and experience they bring to the board, such that it is clear from director information the basis of the assessment of the board's skill matrix

Climate change disclosure and communication	• Consistent, comprehensive and complete climate change disclosures and communication across all channels used to communicate to investors
	• Prepare TCFD reporting that:
	    ○ Provides a thorough overview of the company's governance, strategy, processes for managing climate-related risks, and performance with respect to managing climate-related risks
	    ○ Considers all climate change risks and opportunities
	    ○ Presents information in sufficient detail and sets targets, including emission reduction targets that can be used to assess performance of the company
	    ○ Considers and addresses the different time frames and types of impacts
	    ○ Communicates financial information which is sufficiently granular and serves the needs of a range of financial sector users
	    ○ Explains any changes in approach
	    ○ Includes robust scenario analysis, including a 1.5°C scenario and clearly articulates assumptions made about technology, policy and market conditions
	    ○ Identifies the current and future capital expenditure or investments that are inconsistent with achieving a 1.5°C scenario
	    ○ Presented to investors through the mainstream channels used to communicate to investors

	• Climate reporting should be incorporated into the company's financial statements using the financial metrics typically used by the company, e.g., Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA)

While some investor expectations may go beyond what the Standards may practically require through disclosure, and some may be more relevant to company engagement, they are a good proxy for the needs of a core primary user.

Specifying disclosure of board climate skills in the Standards would also strengthen the broader corporate governance regime in New Zealand, which already advocates for boards to have a balance of skills, knowledge, experience, independence and perspectives, and that "reporting should include information about each director."[20] Climate change is one of a number of skills that any reasonable investor would consider in the context of a broader mix of existing board skills and the business context of the entity, and should expect a board to provide as part of the information about each director.

IGCC believes the XRB's overarching concern can be mitigated by asking reporting entities to define the required board skills to its operations and whether climate expertise is deemed as required or not based on materiality. The entity should then assess current director skills against the broader skills matrix, including climate change. The entire board skills matrix and assessment of directors should then be disclosed. Alternatively, if the XRB is of the view it cannot require the disclosure of a full matrix as part of the Standards, it should require just the climate-related elements of this process be disclosed, including whether climate change is a skill the board has identified as required and what percentage, if any, of the current board have climate-related skills, and who they are. The XRB has indicated it is working up a definition of materiality for the purpose of the Standards, which could be integrated into this section to guide those entities who do not believe climate skills are relevant to their board mix.

IGCC recommends that for the purpose of the Standards a definition of "climate change skills" also be developed drawing from the *World Economic Forum Climate Governance Principle,*[21] *Changing Climate* and the soon to be released work of Cluster 4 of the European Financial Reporting Advisory Group's sustainability reporting standards roadmap, as flagged in its climate prototype working paper,[22] along with other relevant sources. We note some companies have already started to include definitions of climate change skills in their own disclosure, for example see Woodside,[23] and that a standard definition of this term would provide for more comparable reporting as this disclosure practice becomes more common.

We note adopting this approach on skills disclosure would also be broadly consistent with clause 4(c) of the Climate Protocols which asks reporting entities to disclose: "how the body ensures that the correct skills and competencies are available to oversee strategies designed to respond to climate-related risks and opportunities".[24] It would be also consistent with emerging practice in at least Europe, and therefore based

---

[20] https://www.fma.govt.nz/assets/Guidance/180228-Corporate-Governance-Handbook-2018.pdf

[21] https://www.weforum.org/whitepapers/how-to-set-up-effective-climate-governance-on-corporate-boards-guiding-principles-and-questions

[22] https://www.efrag.org/Assets/Download?assetUrl=%2Fsites%2Fwebpublishing%2FSiteAssets%2FEFRAG%2520PTF-ESRS%2520Climate%2520standard%2520prototype%2520working%2520paper.pdf

[23] https://files.woodside/docs/default-source/investor-documents/major-reports-(static-pdfs)/2020-full-year-results-and-annual-report/corporate-governance-statement.pdf

[24] https://www.ifrs.org/content/dam/ifrs/groups/trwg/trwg-climate-related-disclosures-prototype.pdf

on the principle stated above that New Zealand's regime should be compatible both with global minimum prototypes and also emerging practice in other relevant markets.[25]

Recommendations:

- **The reporting entity should be required to disclose its identified and current board skills by publishing a matrix, with climate change being a skill that directors are assessed against if deemed material.**
- **Define 'climate change skills' as it relates to boards and management in the Standards and use guidance to address the perceived risk of adding a disclosure on specific board skills and competencies might inadvertently create an expectation that all boards should have specific climate expertise resulting in a 'shopping list' for directors' expertise.**
- **If the XRB does not believe the Standards should require publication of a full board skills matrix, then reporting entities should be asked to identify whether climate change is a skill needed as part of the mix of skills the board requires to oversee the organisation. If so, the reporting entity should state those director/s it believes have these skills, and if none, how it intends to bring these skills onto the board (through appointments, training or standing external expertise). If climate change is not deemed a relevant board skill the entity should then disclose why.**
- **Add "and how they are assessed" to the end of the clause at 4(c)**
- **Add "strategy" to the clause at 4(e) where it states, "governance and decision making"**
- **Align clause 5(c) with 4(a) by adding "frequency" in 5(c)**
- **Consider adding governance metrics such as the frequency of meetings and workshops on climate change, proportion of time or number of board meetings allocated to the issue, renumeration, performance and financial incentives. This could also be encouraged in guidance.**

3) Do you think the proposed Risk Management section of NZ CS 1 meets primary user needs?

a) Do you think that the information provided under this section of NZ CS 1 will provide information that is useful for decision making to primary users (existing and potential investors, lenders and insurance underwriters)? If not, please explain why not and identify any alternative proposals.

b) Do you consider that this section of the standard is clear and unambiguous in terms of the information to be disclosed? If not, how could clarity be improved?

c) Do you consider that this section of the standard is adequately comprehensive and achieves the right balance in terms of prescriptiveness and specificity? If not, what should be removed or added to achieve a better balance?

IGCC is largely supportive of the approach the XRB has taken in the Risk Management section. Again, the specificity of separating out the tools, processes, timeframes and value chains being used is important and should be included in the final version of the Standards.

IGCC understands the XRB position about being too prescriptive in terms of recommending the specific risks to be assessed against and notes the approach it has adopted is relatively consistent with the Climate

[25] https://www.efrag.org/Assets/Download?assetUrl=%2Fsites%2Fwebpublishing%2FSiteAssets%2FEFRAG%2520PTF-ESRS%2520Climate%2520standard%2520prototype%2520working%2520paper.pdf

Prototype. It may still be useful to include this level of detail in NZ CS 2 or other guidance as a non-exhaustive list and with descriptors of what these risks entail.

CS 1 could also include a requirement for a reporting entity to disclose what potential climate risks it did assess alongside the process for identifying and prioritising risks. This would give investors some confidence that a reporting entity has assessed all relevant risks, even if they were found not to be an issue or a low priority. This would be a separate process to detailing those risks identified as material in the Strategy section.

While Section 5 appears to be about ensuring disclosure of how an entity prioritises risks, especially 5(b), the XRB might want to consider making this intent clearer. In this light, the clause at 11(b)(ii) of the Climate Prototype might be instructive.

Importantly, investors have indicated they want a much clearer demonstration from companies of how the identification and disclosure of climate risks and opportunities are being integrated into overall business strategy. Therefore, the interaction between the Risk Management and Strategy sections of the Standards will be important. IGCC may provide further feedback on Risk Management when the Strategy section is open for consultation in 2022.

Recommendations:

- **Consider adding a requirement to report the types of climate-related risks that were assessed by the reporting entity alongside the process for identifying the risks. This would be separate to setting out the identified material risks in Strategy reporting.**
- **Consider whether Section 5 could be more explicit in asking for disclosure on how a reporting entity *prioritises* different risks.**

4) The XRB has primarily drawn from the TCFD's definitions for its defined terms. Do you agree that we should align closely with the TCFD's definitions?

5) The XRB is particularly interested in feedback on the following defined terms as they are currently proposed: 'climate-related risk', 'climate-related opportunities', 'climate-related issues', 'physical risk', and 'transition risk'.

a) Do you consider that the XRB should align with the TCFD and use the terms 'climate-related opportunities' and 'climate-related issues', or should we only refer to 'climate-related risks'?

b) Do you consider that the proposed definitions for these terms are accurate, sufficiently clear and well-explained? Do they need further detail or explanation? If so, should that detail be included in the defined terms or in guidance?

6) Do you have any other views on the defined terms as they are currently proposed?

IGCC supports the XRB's approach to primarily draw the defined terms from the TCFD, and the definitions as proposed.

As noted above, IGCC recommends the XRB develop a defined term for "climate change skills" as it relates to boards and management. This is because this term is likely to become more common as reporting on board and management processes and skills increases due to the Standards, investor pressure and other practice. An established standard definition for the term would help avoid market fragmentation on its meaning.

Recommendations:

- **Maintain current definitions**
- **Establish a definition for "climate change skills" as it relates to boards and management based on the *World Economic Forum Climate Governance Principles, Changing Climate,* Cluster 4 of the European Financial Reporting Advisory Group's sustainability reporting standards roadmap, and other relevant sources.**

7) The XRB is currently of the view that adoption provisions for some of the specific disclosures in NZ CS 1 will be required. However, the XRB does not believe it is necessary to provide any adoption provisions for entities in relation to the Governance and Risk Management disclosures. Do you agree with this view? Why or why not?

IGCC supports this approach and notes that industry guidance to be released by the XRB alongside the Standards should be enough for these sections.

Recommendation:

- **Maintain proposed approach**

8) The XRB currently intends NZ CS 1 to be concise and sector neutral, with sector specific requirements to be contained in guidance. Do you agree with this approach?

IGCC supports this approach. This is the model that is incorporated to a degree in the Climate Protocols.

Recommendation:

- **Maintain proposed approach**

9) Do you have any other comments?

As noted above, IGCC strongly supports the XRB's sentiments in the Consultation Document that disclosure should not be treated by reporting entities as a compliance exercise. But without disclosure requirements being linked to an actual objective or target, it can lead to reporting becoming a box ticking exercise. New Zealand has legislated commitments and targets on climate change under The Act, as amended by Climate Change Response (Zero Carbon) Amendment Act 2019***.*** In its further work on building out the full Standards and associated guidance the XRB should consider how to embed the objectives of The Act either in the Standards themselves and/or the associated guidance.

As also noted above, IGCC believes that disclosure standards should be reviewed and updated via an iterative process to ensure that the practice driven by that the New Zealand Standards does not fall behind global best practice. Falling behind global practice would risk making the New Zealand economy less competitive as global capital markets will demand the same climate risk information as they can get in other economies. At the same time reporting entities need a stable regulatory environment to report against to guard against unnecessary disruption and red tape. Therefore, it would be useful if a timeline were set out stating how the XRB intends to review and update both guidance and the Standards, if at all.

The New Zealand mandatory climate-disclosure regime does not currently cover unlisted companies and certain other entities including some government and smaller companies. As noted by many actors this could create perverse outcomes such as potentially providing a disincentive to market listing while also creating potential blind spots for regulators charged with overseeing financial stability and climate risk.[26] The XRB does not have a legislative signal to create Standards for reporting by entities not specified in the Bill. However, as market expectations shift, climate risk reporting by these uncovered entities will likely increase, and in turn these entities will likely turn to the Standards to help guide their practice. In this light the XRB could consider further guidance, perhaps once mandatory reporting has started, for voluntary reporting by unlisted companies and other uncovered entities based on the Standards.

Recommendations:

- **Set out a timeline for expected reviews and updates of the Standards and associated guidance.**
- **Consider further specific guidance for the voluntary use of the Standards by unlisted companies and other uncovered entities.**
- **Consider how to explicitly align the Standards and guidance to the objectives of the The Act.**

Conclusion

The proposed Government and Risk Management sections of the Standards largely get the balance right between the required specificity, strength and usability needed to drive consistent and credible climate risk reporting in these two sections. IGCC also supports the broad structure of the Standards and the mix of guidance that is being proposed.

As a priority, IGCC encourages the XRB to consider how to align the Standards and guidance with The Act, as amended by the Climate Change Response (Zero Carbon) Amendment Act 2019.

The IGCC suggests maintaining the level of specificity contained in the Consultation Document in the final Standards. For the Strategy and Metrics and Targets sections, IGCC supports identifying clear expectations on the specific types of cross-sector metrics and the characteristics of scenarios to be used by reporting entities, consistent with developments internationally from the TCFD[27] and the needs of investors for consistent and comparable data as outlined in *Full Disclosure*.

The proposed Governance section should be amended to drive better disclosure from reporting entities on board skills, including reporting of climate skills against individual directors. While this is not currently an explicit part of international standards like the Climate Prototype, it has become a key need of investors (as evidenced in both *Full Disclosure* and *Changing Climate*) and is emerging as a component of potential standards in other markets including in Europe. It is therefore likely to be a feature of governance reporting in many jurisdictions by the time mandatory reporting begins in New Zealand. Strengthening board skills disclosure requirements would also reflect what is regarded as good corporate governance practice in New Zealand regulator guidance.

As noted above, IGCC believes disclosure standards should be built on three broad principles: they are globally comparable; they are reviewed iteratively; and they drive better practice. To aid the first of these principles IGCC has commissioned consultants Te Whakahaere to conduct a global review of disclosure

[26] https://www.minterellison.co.nz/our-view/new-zealand-to-lead-the-world-in-climate-related-financial-disclosure
[27] https://assets.bbhub.io/company/sites/60/2021/07/2021-Metrics_Targets_Guidance-1.pdf

regimes to determine where common landing areas on different themes are emerging, where there is divergence, and how this might be relevant to the development of the Standards. This research should be available to the XRB and others in late-December. The findings of this work and other international developments may further shape IGCC's views and recommendations on the Governance and Risk Management sections of the Standards in later consultations.

Recognising the value in a common global baseline for comparability of disclosures, IGCC supports the XRB's intention to review baseline-level alignment with IFRS standards under development in the process of developing the draft and final XRB Standards.

IGCC thanks the XRB for the opportunity to provide comments on the Consultation Document and stands ready to assist as it develops the next sections of the Standards (i.e. NZ CS 1), NZ CS 2 and the associated guidance.