



Boutique Investment Group submission on: XRB Strategy and Metrics and Targets sections, Aotearoa New Zealand Climate Standard 1: Climate-related Disclosures (NZ CS 1)

Submitted by the Boutique Investment Group on behalf of: AMP Wealth Management New Zealand Limited; Always Ethical Limited; Castle Point Funds Management; Fisher Funds Management Limited; Kiwi Wealth Investments Limited Partnership; Milford Funds Limited; Mint Asset Management Limited; Nikko Asset Management New Zealand Limited; Pie Funds Management Limited; and Salt Investment Funds Limited.

INTRODUCTION AND OVERVIEW OF SUBMISSION

We are pleased to make this submission on behalf of the above listed managers of retail managed investment schemes via the Boutique Investment Group (BIG).

As the XRB is aware, retail fund managers are in a different position to other types of climate reporting entities in that:

- Our customers invest in the funds that we offer, rather than in us as an entity. Consequently, the climate risks and opportunities that investors will want to hear about are those that sit within the funds that they have invested in, rather than us as businesses, (especially as our own climate profiles will be those of any other vanilla corporate office). The only real situation where our own business strategy would be relevant is where we have committed to some form of general position that will flow into all the funds in a material way. For example if a business were to commit to having all funds with a net carbon zero status by 2050, then that would be relevant to disclose as that would flow through into the management of funds.
- All the climate change risk and data that is relevant to investors in managed funds can only be sourced from third party entities or data aggregators, rather than from ourselves. Therefore we are totally reliant on third party entities' disclosures to produce our reports. This has several implications including that; there is an ongoing risk that portfolio level statistics can be misleading when not all the investee companies report and so are removed from both the numerator and denominator; and the matters that we can report on are limited by the data that global data aggregators offer. The upside of there only being a handful of data aggregators is that it will naturally impose a level of consistency in the reporting by fund managers.
- All the climate change risk and opportunity within a fund, will likely be spread across many different investee businesses. Therefore a key question will be how deeply we need to drill into any particular investee business in order to reasonably convey the climate risk within a fund. This is relevant to our discussion of scenarios as well as to targets and metrics.

- To the extent that we are invested in highly liquid securities that can be disposed of for the right price immediately, we are always free to opt out of the climate risks of any of the businesses that we invest in, so we are arguably not locked into the same kind of climate journey as other businesses. For example, if a fund manager were to buy shares in Z Energy in the expectation of it being subject to a takeover offer within a few months, this is not the same as actually being Z Energy and facing Z Energy's issues for the long haul. (This is not to say many fund managers do not take ESG considerations, such as long-term climate risks into account. It is just an observation that our investors may not truly face the risks inherent within the businesses that we invest because of our investment time horizons.)

We seek clarifications to the standards to acknowledge these points.

Further high level remarks

1. Relevance of material for primary users

- The majority of primary users for the managers of investment schemes are retail investors via KiwiSaver or direct investment schemes. For example, the FMA's "KiwiSaver Annual Report 2021" records that there were 3,090,631 New Zealanders invested in KiwiSaver as at 31 March 2021, which is the majority of the New Zealand workforce.
- These primary users, who will be ordinary people for the most part will not want to pick their way through a highly technical report. Reporting should be minimal, meaningful and engaging.
- It is also worth remembering that the costs of this reporting will ultimately be paid for by investors, rather than other kinds of reader.
- Accordingly we feel that reporting requirements, both in the Strategy and Metrics and Targets section, are too technical and too large in volume to meet the needs of these primary users. The statements and reminders to entities to "apply judgement when applying the disclosure requirements and not to obscure relevant information by the inclusion of insignificant detail" seems almost paradoxical when looking at the depth of information being asked for in the Metrics and Targets section in the context of the retail investor as the primary user. In our view NZ CS 1 needs to build in some kind of acknowledgement that not all primary users will be relevant to all Climate Reporting Entities (so that we can focus on relevant primary users i.e. retail investors and not irrelevant primary users e.g. underwriters/Lloyds).
- To reiterate the points above, we refer to FMA reports¹ produced in 2014 and 2018 on improvements in the presentation of financial statements. These reports acknowledge that disclosure overload in financial statements can obscure more pertinent information and therefore detract from their usefulness and relevance. We question whether primary users will be in a better position to make well-informed investment decisions given the level of detail and the very technical nature of the proposed climate-related disclosures.

2. Guidance needed on level of detail of reporting

- Associated with the point above, a climate report on a fund could at one end of the spectrum provide some high-level commentary on how different kinds of business within the portfolio may behave in different climate scenarios, or at the other provide technical

¹ *Quality Financial Reporting and Improving Financial Statements*

breakdowns of every investee company within the portfolio. (It is not clear that a detailed breakdown would provide significantly more value to the average reader and in fact may serve only to disengage). Therefore, a critical piece in providing comfort around the climate reporting requirements is some guidance as to what the level of detail needs to be for the readership. Such guidance would not only be useful for those tasked with producing the reports, but also those tasked with auditing the reports.

3. A crystal clear statement of what we are trying to achieve with our climate reporting

- There still remains some confusion as to what a climate report is intended to achieve.

Climate Standard 19B states:

19B Purpose of climate standards and climate-related disclosures

The purpose of climate standards is to provide for, or promote, climate-related disclosures, in order to—

- (a) encourage entities to routinely consider the short-, medium-, and long-term risks and opportunities that climate change presents for the activities of the entity or the entity's group; and
- (b) enable entities to show how they are considering those risks and opportunities; and
- (c) enable investors and other stakeholders to assess the merits of how entities are considering those risks and opportunities.

And new section 461Z of the FMC Act States:

Climate statements relating to registered schemes

461Z Climate statements for separate funds of registered schemes, etc

- (1) This section applies to every manager of a registered scheme that is a climate reporting entity in respect of the scheme.
- (2) The manager must ensure that, within 4 months after the balance date of the scheme, climate statements that comply with applicable climate standards are—
 - (a) completed in relation to each separate fund of the scheme and that balance date; and
 - (b) if any liabilities of the manager and the scheme are not limited to a separate fund, completed in relation to the scheme and that balance date; and
 - (c) dated and signed on behalf of the manager by 2 directors of the manager or, if the manager has only 1 director, by that director.

- Our readings of these provisions is that the intent of requiring us to report in relation to each separate fund is that the report needs to tell the reader how we are thinking about the topics listed in clause 19B insofar as they relate to the activities of the fund.
- As was our feedback on the Governance and Risk Management standards, the Strategy and Metrics and Targets sections speak more to disclosures in relation to a corporate entity and its business, rather than the retail investment schemes that are the target of reporting for MIS managers. It is unclear how to apply the standards to MIS reporting and we request clarity on this matter. One example is the reference to “financial planning” in Strategy section 6.2, but this flavour runs through all of the content that is under consultation. Where a MIS manager makes an assessment regarding the extent to which it is impacted by climate-change, will the justification for this assessment need to be included in the disclosures? Will the justification need to be validated by an independent third party?

4 Availability of data

- It will only be possible to collate and report the data required for the Metrics and Targets section using an external ESG data platform.
- Mainstream providers of this data are currently MSCI, Sustainalytics, S&P Global and Bloomberg.
- These providers do not yet provide climate-related opportunities or capital deployment data. Transition risk and physical risk data is not comprehensive or useful (for example the physical risk data provided by S&P Global has only 70.95% of holdings covered on one typical, global multi-asset fund analysed, with the result a composite score that is not meaningful to primary users). It is unclear if this data will be available, comprehensive or of high enough quality to provide to primary users by the reporting date.
- In many instances the requirement is to provide “actual” data (for example in Strategy 5(c) – requirement is to provide “actual” financial impacts of climate related risks and opportunities on financial position, financial performance and cashflows) and we do not believe that this will be available in respect of portfolio investee companies.

Data for New Zealand listed companies will become available for MIS managers to use in the year following our first climate disclosure statement (and we understand the transitional provisions will address this delay). We note disclosures will not be required for offshore companies until a later date.

Specific comments

	Strategy	
1.	<p>Do you think the proposed Strategy section of NZ CS 1 meets primary user needs?</p> <p>(a) Do you think that the information in this section of the standard will provide information that is useful to primary users for decision making? If not, please explain why not and identify any alternative proposals.</p> <p>(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?</p> <p>(c) Do you consider that this section of the standard is adequately comprehensive and achieves the right balance between</p>	<p>The volume and technical aspect of these requirements make them unsuitable for the needs of our primary users.</p> <p>As noted above the industry needs further guidance about the level of detail that must go into the reporting.</p> <p>Please see existing reporting examples from the managers of investment schemes.</p>

	prescriptiveness and principles-based disclosures? If not, what should be removed or added to achieve a better balance?	
2.	Do you agree that a standalone disclosure describing the entity's business model and strategy is necessary? Why or why not?	We do not have a strong view but understand this could be helpful for some primary users.
3.	Do you agree that we should not prescribe which global mean temperature increase scenario(s) should be used to explore higher physical risk scenarios (such as 2.7°C and/or 3.3°C or by using Representative Concentration Pathways (RCP) such as RCP4.5 or 6), but rather leave this more open by requiring a 'greater than 2°C scenario'? Why or why not?	Managers of investment schemes will not be able to collate the data provided by underlying companies if: <ul style="list-style-type: none"> a) Scenarios are not consistent b) All companies are not required to disclose scenario requirements c) This data is not aggregated into a usable format. As such, it is inevitable managers of investment schemes will have to calculate this data from scratch for every underlying company investment. This will require the use of an external ESG data provider. Therefore, the flexibility to decide which temperatures to use in scenario analysis will assist the selection and use of external data providers given they may not all align with mandated temperatures.
4.	We do not require transition plans to be tied to any particular target such as net zero and/or 1.5°C, but that entities will be free to disclose this if they have done so. Do you agree? Why or why not?	The more flexibility provided the better..
5.	Do you have any views on the defined terms as they are currently proposed?	See below.
6.	The XRB has identified adoption provisions for some of the specific disclosures in NZ CS 1: (a) Do you agree with the proposed first-time adoption provisions? Why or why not? (b) In your view, is first-time adoption relief needed for any of the other disclosure requirements? Please specify the disclosure and provide a reason. (c) If you are requesting further first-time adoption relief, what information would you be able to provide in the interim?	There appears to be significant overlap between transition and adoption plans for managers of investment schemes under the current definitions provided. If 1 yr relief is provided for the transition plan and 2 yr relief is provided for the adaption plan, more clarity between these two plans would be helpful.
		This whole first time adoption section is unclear and needs to be rewritten or provided with more guidance/examples. Need to remove all requirements for calculating scenario outcomes on scope 3 as the data and tools are not reliable/robust.
	Other comments on Strategy	The treatment of commercially sensitive climate related opportunities needs to be considered. There is currently no suggestion in the standard that we can withhold a level of detail here to be able to protect our commercial position and competition in the sector - and we believe we should be able to.

		Strategy 5c and 6c: we seek clarity over which reporting periods or horizons for which the entity needs to calculate and provide this disclosure.
		Strategy 7 – methodologies and assumptions – this section contains a high degree of prescription for something that is meant to be principles based. For example, 7(a)(iii) – pathways, assumptions, macro-economic trends etc etc. This is a lot more detailed than TCFD. This reinforces the point about retail primary users not finding this information useful.
		Strategy 7(a)(iii): To ensure comparability across reporting entities, we recommend the XRB publish a set of standardised pathways and assumptions.

	Metrics and Targets	
7.	<p>Do you think the proposed Metrics and Targets section of NZ CS 1 meets primary user needs?</p> <p>(a) Do you think that the information in this section of the standard will provide information that is useful to primary users for decision making? If not, please explain why not and identify any alternative proposals.</p> <p>(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?</p> <p>(c) Do you consider that this section of the standard is adequately comprehensive and achieves the right balance between prescriptiveness and principles-based disclosures? If not, what should be removed or added to achieve a better balance?</p>	<p>The volume and technical aspect of these requirements make them unsuitable for the needs of our primary users.</p>
8.	<p>We have not specified industry specific metrics. The guidance will direct preparers where to look for industry-specific metrics.</p> <p>Do you believe this is reasonable or do you believe we should include a list of required metrics by industry?</p> <p>If so, do you believe we should use the TCFD recommendations or follow the TRWG prototype?</p>	<p>There is a wide scope for reporting provisions for managers of investment schemes.</p> <p>TCFD and TRWG are not suited to managers of investment schemes in the Strategy or Metrics and Targets sections.</p> <p>More guidance for this group, such as minimum required standards, would be useful. We also seek guidance on the types of consolidation methods to use.</p>
9.	<p>We will require disclosure of scope 3 value chain emissions as part of this standard.</p> <p>Are there areas (particularly in your scope 3 value chain) where there are impediments to measuring at present?</p> <p>If so, what are these areas and when do you think it might be possible to measure these areas?</p>	<p>Scope 3 data has poor coverage and large inaccuracies for managers of investment schemes. In particular, scope 3 downstream data is rarely reported. If reporting has very large parts of the data missing then it will be misleading, at best.</p>
10.	<p>Paragraphs 8, 9 and 10 contain specific requirements relating to the disclosure of GHG emissions to facilitate the conduct of assurance engagements in line with the requirement of</p>	

	section 461ZH of the Financial Markets Conduct Act. Do you have any observations or concerns about these proposed requirements?	
11.	Do you have any views on the defined terms as they are currently proposed?	Our view is that “science based” needs to be defined.
12.	The XRB has proposed not providing first-time adoption provisions for the Metrics and Targets section of NZ CS 1. Do you agree? Why or why not?	We would again point to availability issues with data. At a minimum, further adoption provisions for the following will be required: <ul style="list-style-type: none"> • climate-related opportunities • deployment data • comparative data • actual scope 3 emissions data
	Other comments on Metrics and Targets	Metrics and Targets 8 - specifically around the GHG emissions of the climate reporting entity . We are required to produce climate statements for each scheme (or separate fund, if applicable), however the standard as written requires emissions of the entity . It is unclear how to apply this to MIS managers.
		Metrics and Targets 9 – GHG emissions report with full data underlying the Climate Statement disclosures: it is unclear what this report must contain and what other requirements we must meet. We assume that it will not need to be lodged on the Disclose Register as there does not appear to be a legal obligation to do so – and assume that it will only be required to be included on our website. Is this what XRB is expecting?
	Assurance	
	Assurance – The XRB proposes that the minimum level of assurance for GHG emissions be set at limited assurance. Do you agree?	We agree with limited assurance.
	Materiality	
	Definition of “materiality”: <i>(Information is material if omitting, misstating, or obscuring it could reasonably be expected to influence decisions that primary users make on the basis of their assessments of an entity’s enterprise value across all time horizons, including the long term)</i>	This definition is fairly meaningless in the context of retail investors – we do not expect they will make assessments of enterprise value across time horizons
	Paragraph 5 of draft CS3/Materiality – requirement to include additional disclosures if material:	The requirement to include additional disclosures further to the content required under the Climate Standards “if that information is necessary for primary users to understand” feels onerous. Primary users of Climate Statements from fund managers (ie retail investors) will have a vast range of knowledge and capabilities, so it is very hard to know what additional information may be required – in most cases the level of understanding of the Climate Statements’ technical detail will be low. If there is a base level of additional info XRB thinks is required to help primary users understand, then we suggest that

		this is explicitly identified to ensure consistency across the industry.
	Table 10/Section 9.1 of the consultation document – Proposed key content of CS3 to include sections on “fair presentation” and “qualitative characteristics of useful information”	These proposed sections of CS3 will require “ faithful representation ” of information, being information that is “ complete, neutral, and free from error ”. These are new concepts and I suggest that they are dropped in favour of already familiar concepts such as those in the fair dealing provisions of part 2 FMCA (which are that representations are substantiated, and that information published is not misleading, deceptive, confusing or likely to mislead, deceive or confuse). Currently it is unclear how the “faithful representation” requirement is supposed to sit alongside Part 2 FMCA (which will seemingly already apply to the Climate Standards we produce anyway).

Inequity of costs

As a final comment, we do not yet know with precision what the costs of the climate reporting regime will be. However, between growing our in-house capability, paying for access to data and paying for assurance across multiple funds, it is likely that there will be a material cost burden for someone pay. The parties most likely to carry that burden will be the investors.

It is an interesting point that while the investors will be paying the costs of the reporting, there are other parties not contributing to the costs also, claiming to be stakeholders. Therefore, baked into the regime is a degree of inequity in that the people wanting to use the reports are not the same as those who are likely to be paying for its costs.

To keep the inequity to a minimum, it would make sense to avoid gold plating the obligations as much as possible, avoid duplication of work and cost between parties as much as possible, and recognise the investors as the primary audience for the reporting.