UK FINANCE

Enhancing climate-related disclosures by standard listed companies

UK Finance response to the FCA Consultation Paper CP 21/18

10 September 2021

Overview

UK Finance is the collective voice for the banking and finance industry operating within the UK. Representing around 300 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation.

Sustainability is one of our six strategic priorities. We are wholly supportive of the UK's goal to achieve net zero emissions by 2050, as well as the interim targets set out in the carbon budgets, and recognise the important role for the banking and finance sector in this historic transition. Our Board in May passed a resolution expressing support in principle for the global Net Zero Banking Alliance (NZBA), formed as part of the Glasgow Financial Alliance for Net Zero (GFANZ) announced only the month before, and encouraging all members to embed climate responsibility into their governance and strategy in support of whole economy transition to net zero by 2050 premised upon *just transition* principles.

TCFD reporting is central to this historic transition, and something we have endorsed previously, such in our response on 5 May to the BEIS consultation on Mandatory climate-related financial disclosures by publicly quoted companies, large private companies and LLPs and our response on 1 October 2020 to the FCA consultation on enhancing climate-related disclosures by premium listed companies. Likewise, we are broadly in support of the initiative to regulate for climate-related financial disclosures by standard listed companies, and welcome many of the proposals in this Consultation Paper.

There are, however, issues arising from the consultation that we believe need thinking through carefully, as set out below. Our response to question 3 in particular indicates that our members are not supportive, at this point in time, of extending TCFD disclosure requirements to listed debt on UK exchanges.

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Response to the discussion paper questions

Proposals to extend climate-related disclosure requirements to certain standard listed companies

Scope

1. **Do you agree with our proposal to extend the application of our existing TCFD-aligned disclosure requirement (set out in LR 9.8.6R(8)) to issuers of standard listed equity shares, excluding standard listed investment entities and shell companies? If not, what alternative scope would you consider to be appropriate, and why?**

Yes, we agree. This is an important, timely milestone towards the goal of full TCFD coverage of the global economy, which will enable the realisation of Mark Carney's vision that every financial decision takes climate change into account.

However at least one member has expressed the view that disclosure should be at the group level only and without requiring separate disclosures for a subsidiary company (an approach consistent with the recent BEIS consultation process on proposed TCFD-aligned disclosures for certain UK companies and LLPs).

2. **Do you consider that issuers of standard listed GDRs and standard listed issuers of shares other than equity shares should also be subject to our TCFD-aligned disclosure requirements? If not, what alternative approach would you consider to be appropriate, and why?**

Yes, we agree.

3. **We welcome views from market participants on whether to apply TCFD-aligned disclosure rules to issuers of standard listed debt (and debt-like) securities, and how best to do this. In particular, we seek input on the following:**
    a. **What climate-related information from issuers of these securities would market participants find decision useful and how far would these information needs be met by TCFD-aligned disclosures?**

    b. **Do market participants' information needs differ according to the different types of issuer in LR 17?**

    c. **If you consider that we should apply TCFD-aligned disclosures rules to issuers of standard listed debt (and debt-like) securities, should some issuer types be excluded from the rule to deliver an effective and proportionate approach? If so, which types of issuers should be included/excluded and how can the scope best be defined?**

We are not supportive, at this point in time, of extending TCFD disclosure requirements to listed debt on UK exchanges. Including listed debt would be materially disruptive to non-UK firms that issue Euromoney Medium Term Notes, and other offshore issuance programmes, and choose to list in the UK. Such a move would likely result in lower debt listings in the UK, undermining the UK's role as a global financial centre.

In addition for non-UK firms that have listed debt securities in the UK and that currently issue a TCFD disclosure, the more prescriptive approach of requiring disclosure along the

TCFD recommendations, as opposed to the TCFD principles, would in many cases prove highly challenging. This is because such non-UK firms disclosures in most cases are aligned to the principles. While this may be a requirement under the rules applying to premium listed firms, this is very different to the circumstances here. We would encourage ongoing monitoring of TCFD disclosure coverage for listed securities in the UK and adoption in other jurisdictions, before any extension to listed debt securities.

d. **Are there any other matters we should take into consideration – e.g., competitiveness, complexity of the application of the rule, burden on issuers in LR 17, or the feasibility to comply with any potential rules?**

We believe that disclosure at the group level is appropriate. This would mean that a subsidiary company rely on the global parent company's disclosure rather than requiring separate disclosures for a subsidiary company, which seems appropriate given that issuance of debt and equity is most typically conducted via the global parent company rather than at subsidiary level.

Design of the proposed Listing Rule

4. **Do you agree with our proposal to mirror the structure and wording of LR 9.8.6R(8) and LR 9.8.6BG to LR 9.8.6EG for companies with a UK premium listing? If not, what alternative approach would you consider to be appropriate, and why?**

Yes.

5. **Do you agree that, subject to the TCFD's final guidance materials being broadly consistent with those proposed, we should incorporate them into our existing and proposed handbook guidance provisions as described (including both the existing guidance relating to LR 9.8.6R(8) and our proposed new guidance relating to LR 14.3.27R):**
    a. **the TCFD's proposed updates to the TCFD Final Report and TCFD Annex**

Yes.

b. **the TCFD's proposed standalone guidance document on metrics, targets and transition planning**

Yes. However while we broadly support aspects of the proposed disclosure guidance e.g. climate-related metrics, and believe that these will add value over time, there needs to be a clearly defined implementation timeline, particularly given the binding status that the requirements are rapidly acquiring. This should allow for reliable, high quality data to become available and facilitate meaningful industry disclosures.

c. **the TCFD's technical supplement on measuring portfolio alignment. If not, what alternative approach would you prefer?**

Possibly, though we would need to review the final version of the supplement before endorsing it. We responded to a TCFD consultation on forward looking metrics in January urging caution in placing weight on portfolio alignment metrics given their immaturity and the many hurdles to be overcome in order for them to become reliable and decision-useful. Whilst portfolio alignment metrics offer significant benefits in theory, we see significant risks in premature regulatory reliance on these metrics. There are some serious impediments to

the usefulness of portfolio alignment metrics for TCFD disclosure and we would urge caution in seeking adoption. If adopted, there needs to be additional transparency about the methodology used, as the connection between carbon intensity and the implied temperature rise can be highly variable between methodologies and present a misleading impression of a portfolio's alignment to climate change outcomes.

6. **Do you agree that we should update the Technical Note 801.1 to reflect the proposed new rule and associated guidance in this CP?**

Yes, though as noted in response to question 5.c. above, the Technical Note should not reflect the latest TCFD guidance wholesale if that guidance could be improved upon, as may be the case regarding portfolio alignment.

SASB metrics

7. **Do you agree with our encouraging listed companies to consider the SASB metrics for their sector when making their disclosures against the TCFD's recommended disclosures, as appropriate? If not, please explain.**

There are numerous industry frameworks, including CDP, GRI, IIRC and SASB, which are either adopted or in the process of being adopted for disclosures. Significant effort has already been invested in their development, and yet work to develop international consistency continues.

It is important that standards are internationally applicable. As an example, at present many of the SASB metrics are US-centric, and therefore currently have lower relevance in other jurisdictions. Meanwhile work continues to develop a common international reporting standard for sustainability with both the IFRS Foundation (ISSB) working towards a baseline international reporting standard on sustainability, and the forthcoming TCFD guidance on metrics, targets and transitional planning. These are expected to provide the specificity and granularity towards consistent and comparable disclosures.

In the meantime, we recommend that companies decide which tools best serve their purpose and meet the needs of their key stakeholders. For example, SASB and GRI provide complementary standards for sustainability information. SASB Standards focus on ESG issues expected to have a financially material impact on the company while GRI Standards focuses on the economic, environmental, and social impacts of a company in relation to sustainable development.

Review of the 'comply or explain' compliance basis

8. **Do you agree with our approach to maintain a 'comply or explain' compliance basis until such time as a common international reporting standard has been published and adopted in the UK? If not, what alternative approach would you prefer, and why?**

Yes.

The role of audit and assurance

9. **Do you agree with our approach not to require third party audit and assurance for issuers' climate-related disclosures at this time? If not, what additional requirements would you consider to be appropriate?**

Yes. While we consider third party audit and assurance to be a longer-term objective, we would agree that this should not be mandated at this point in time.

Timing

10. **Do you agree that our new rule should take affect for accounting periods beginning on or after 1 January 2022? If you consider that we should set a different timeframe, please explain why.**

Yes.

11. **Do you agree with the conclusions and analysis set out in our cost benefit analysis (Annex 2)?**

We have no comment.

Discussion topics on ESG integration in UK capital markets

Prospectuses and 'Use of proceeds' Bond Frameworks

12. **If future changes were considered in relation to the UK prospectus regime, we would welcome views on also taking the opportunity to introduce specific requirements in relation to UoP bond frameworks and their sustainability characteristics?**

The consensus among our members is that it is not necessary to introduce new requirements for UoP bonds into the UK Prospectus Regulation at this point in time, because prospectus disclosure for UoP bonds listed and offered in the UK already follows a relatively consistent approach. An estimated 97% of sustainable bonds issued globally in 2020 referenced the Green Bond Principles, the Social Bond Principles or the Sustainability Bond Guidelines.

It may be appropriate to re-visit the question of prospectus requirements for green bonds when an appropriate regulatory regime for green / social / sustainability bond framework verification is established. Please see our response to Q. 15, in which we support a dialogue on the introduction of such a regime.

13. **Should the FCA explore supporting the UoP bond market by recognising existing standards (e.g., ICMA Principles), potentially through our recognition of industry codes criteria and process?**

Having consulted with ICMA, and our membership, our understanding of the FCA industry codes and related processes is that they are intended for unregulated markets in order to prevent any misconduct and that typically standard setters would approach the FCA before drafting any codes. In the case of the Principles, based on the above, we do not think that there is any need for the FCA to get involved for the purpose of tackling any serious

misconduct in the UoP bond market. Also, FCA recognition would have to be applied to existing standards which would be slightly different to the current process.

In our opinion, the FCA would nonetheless add value to the market through regulatory recognition of the Principles including all of its four constituents, not just the ones for UoP bonds.

14. **We would also welcome views on more ambitious measures the FCA could consider, for example to require that the central elements of UoP bonds be reflected in contractual agreements and set out in the prospectus.**

We have no comment.

The role of verifiers and second party opinion providers

15. **We would welcome views on the potential harm set out above and what, if any, actions the FCA or the Treasury should consider.**

We agree with the potential harms set out in paragraphs 4.25-26, and would support the FCA further considering regulatory proposals to address these. We would look forward to commenting on these proposals in due course.

16. **Should the FCA, alongside the Treasury, consider the development and creation of a UK bond standard, starting with green bonds?**

We believe that the ICMA principles have established a global standard. Therefore our recommendation would be to draw on those principles as much as possible without seeking to interpret them. If anything is needed we would advocate a minimalist piece of regulation which simply puts into statute the need to follow the principles without seeking to translate them or embody them in statute or regulation itself. This aligns with the approach set out in the UK Government Green Financing Framework of June 2021.

In addition to the extent possible any UK green bond standard, if deemed essential, align with the EU Green Bond Regulation, particularly on (i) eligible expenditures and assets (i.e. Article 4 of the European Green Bond regulation), (ii) reporting requirements, and (iii) external review.

For the development of green bond product standards that are aligned to a definition of environmentally sustainable activity (taxonomy), the usability of such a taxonomy should be the foremost consideration. Requiring bespoke data collection for verification is likely to hamper adoption of taxonomies and product standards by market participants. Where possible existing data sources for UK corporates should be utilised, as this would reduce the compliance costs associated with aligning with a UK taxonomy/product standard.

Policy responses

17. **Do you agree with how we have characterised the challenges and potential harms arising from the role played by ESG data and rating providers? If not, please explain what other challenges or harms might arise?**

Yes.

18. **Would further guidance for firms on their use of ESG ratings – and potentially other third-party ESG data – be useful, potentially clarifying expectations on**

outsourcing arrangements, due diligence, disclosure and the use of ratings in benchmarks and indices? Are there other aspects such guidance should include?

Yes, this would be useful.

19. **We would welcome views on whether there is a case either to encourage ESG data and rating providers to adopt a voluntary Best Practice Code, or for the FCA to engage with the Treasury to encourage bringing ESG data and rating providers' activities inside the FCA's regulatory perimeter.**

We can see merit in these proposals being explored and would add that we have been supportive of IOSCO playing a bigger role in the oversight of ESG ratings and data providers.

20. **If there is a case for closer regulatory oversight of ESG data and rating providers, we welcome views on:**
    a. **Whether transparency, governance and management of conflicts of interest are the right aspects of ESG data and rating providers' operations and activities to prioritise in regulatory oversight, and if not, what other aspects should be considered**

Yes, these would be the right areas to focus on.

   b. **Whether and how regulatory priorities should differ between ESG rating providers and other ESG data providers**

   c. **The similarities and differences between the policy issues that arise for ESG rating providers and those that arise for CRAs, and how far these similarities and differences might inform the appropriate policy response**

We have no comment.

Sustainable finance in wider capital markets

21. **What other ESG topics do you consider that we should be prioritising to support our strategic objective? Please explain.**

We have no comment.

For further information on this submission please contact Paul Chisnall, Director, Sustainability, UK Finance (paul.chisnall@ukfinance.org.uk).