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**Technical Expert Group on Sustainable Finance**

**European Commission**

**Directorate-General for Financial Stability, Financial Services and Capital Markets Union**

**European Commission**

**1049 Bruxelles/Brussels**

**Belgium**

**Re: Report on Climate-related Disclosures**

CFA Institute[1] welcomes the opportunity to comment on the European Commission's Technical Expert Group on Sustainable Finance Report on Climate-related Disclosures[2]. We commend the Technical Expert Group on Sustainable Finance ("Technical Expert Group") for their work attempting to help identify material climate change data that will be most useful to issuers, investors and stakeholders.

We have read the European Commission's revised non-binding guidelines (NBGs) of the Non-Financial Reporting Directive (NFRD) concerning disclosure of environmental, social and governance-related information, and wish to share our comments.

The CFA Institute Standards of Professional Conduct require CFA charterholders to conduct appropriate research and investigation of all material information relevant to their investment analyses and portfolio management decisions, recommendations, or actions.

CFA Institute consistently monitors key debates and evolving issues concerning the role and application of environmental, social, and governance (ESG) information in the investment management process. More thorough consideration of ESG factors by financial professionals can improve the fundamental analysis they undertake and ultimately the investment choices they make. CFA Institute is specifically focused on the quality and comparability of the ESG information provided by corporate issuers and how to integrate various ESG factors into the investment selection process.

CFA Institute and Principles for Responsible Investment (PRI) recently set out to create a best practice report (Guidance and Case Studies for ESG Integration: Equities and Fixed Income) and three regional reports [one for the Americas (AMER), one for Asia Pacific (APAC), and one for Europe, the Middle East, and Africa (EMEA)] to help investors understand how they can better integrate ESG factors into

[1] CFA Institute is a global, not-for-profit professional association of over 166,000 investment analysts, advisers, portfolio managers, and other investment professionals in 163 markets, of whom more than 159,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 152 member societies in 74 markets. For more information, visit www.cfainstitute.org.

[2] Report can be found at the following link: https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/190110-sustainable-finance-teg-report-climate-related-disclosures_en.pdf

their equity, corporate bond, and sovereign debt portfolios. While this report focused on broader ESG issues than just climate change, our findings suggested a few important points that are pertinent to the current climate change discussions and the climate related disclosures that are the topic of the Technical Expert Group's report.

Our main findings include the following points:

- There is no "one best way" to do ESG integration and no "silver bullet" to ESG integration.
- The main drivers of ESG integration are risk management and client demand.
- The main barriers to ESG integration are a limited understanding of ESG issues and a lack of comparable ESG data.
- Investors acknowledge that ESG data have come a long way but advances in quality and comparability of data still have a long way to go.

*We therefore support better quality and more consistent ESG and sustainability disclosures. We believe that investors should have access to and consider material ESG information (including material climate related data) as such information can be an important component of a complete and thorough financial analysis for any actively managed fundamental investment portfolio.*

**Comment on 1.3 The Role and Benefits of Climate-related Disclosure**

*We support the Technical Expert Group efforts to improve the quality and consistency of disclosures around climate change and related data. Such data can allow investors increased awareness and understanding of a company's climate risks, risk management, and related strategic planning.*

The Task Force lists the following as some of the potential benefits of climate-related disclosures:

- Better understanding of the exposure of a company's operations to physical and transition risks related to climate change
- Inclusion in actively managed investment portfolios and in sustainability-focused indices, used for passive investment strategies
- Climate-related disclosures used to improve credit ratings for bond issuance and credit worthiness assessment for bank loans
- Reduced friction in investor engagement and shareholder action and voting

*In our discussions with investors we see the need to focus attention on the first bullet point in this list, understanding that the other items listed will follow when investors have the information they need to adequately manage all ESG risks, including climate related risks. Investors consistently tell us that the main drivers of ESG integration in the investment process are risk management and client demand, but that the main challenge is a lack of consistent, verifiable and comparable ESG data.*

**Comment on 1.4 The Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD).**

*We support the efforts of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) to increase transparency in the market around climate-related issues and support broader adoption of the TCFD recommendations.*

**Comment on 1.6 Objective of the report**

The guidance proposed in the Technical Expert Group's report intends to assist companies in developing high quality climate-related disclosures that comply with the European Commission's Non-Financial Reporting Directive (NFRD) and address the recommendations around climate disclosures of the TCFD.

Specific disclosures and guidance are described under each element of the NFRD requirements, including metrics for companies. The proposed guidance included in the report:

1. reference the TCFD recommendations;

2. are supported by standards that companies can turn to for further guidance;

3. address gaps in current reporting practice;

4. enable comparability across jurisdictions;

5. align with the EU's decarbonization efforts; and

6. streamline reporting.

The recommended disclosures included in the report are differentiated based on the level of exposure of reporting companies with respect to climate-related risks and opportunities. Three types of disclosures are suggested:

- Type 1 disclosures – those that companies should disclose (high expectation that all reporting companies disclose them)

- Type 2 disclosures – those that companies should consider disclosing (expected of companies with significant exposure to climate-related risks and opportunities)

- Type 3 disclosures – those that companies may consider disclosing (additional or innovative disclosures that provide more enhanced information)

*CFA Institute agrees that this type of voluntary disclosure model forms a reasonable basis for reporting around climate related issues and could be used as a framework for other ESG related disclosures. We support giving companies the flexibility to disclose the climate data that they feel works best for them. Through such a model we would expect issuers and investors to engage with one another to come to an agreement on which data best fits that issuers current circumstances without the need of a one-size-fits-all regulatory system in place.*

**2. Disclosures Under the Directive: Principles and Rationale for Non-Financial Reporting**

**2.1 Reporting audience**

Reporting under the NFRD is intended “to meet the needs of investors and other stakeholders as well as the need to provide consumers with easy access to information on the impact of businesses on society” whereas the TCFD’s target audience is investors, lenders, and insurance underwriters.

**2.2 Journey of Continuous Improvement in Reporting**

*CFA Institute supports guidelines that identify detailed, yet flexible disclosure elements such as a specific set of climate-related disclosures. Both the TCFD recommendations and other existing reporting frameworks seek to increase consistency and quality of climate-related reporting.*

*We feel, as the Technical Expert Group does, that companies should be encouraged to disclose information in accordance with one or more of the globally-accepted, sustainability reporting frameworks to maximize comparability of material climate data for their investors and stakeholders.*

**2.3 Reporting on Climate Change Impacts**

The TCFD recommendations focus on how the physical effects of climate change and the anticipated transition to a low-carbon and climate-resilient economy impact companies, and ultimately investors. The NFRD has introduced a new element to be taken into account when assessing the relevance of non-financial information by referring to information ‘to the extent necessary for an understanding of the impact of (the company's) activity.’ Companies are required to disclose relevant information on the consequences of climate change for a company’s business complemented with information on the impact of the company on climate change.

This last distinction “… information on the impact of the company on climate change.” Is an important one, as investors and stakeholders alike wish to know the impact that companies in their portfolios will have on climate change, as those with larger impacts may pose more risk (regulatory, market, consumer choices) to their portfolio than companies with a smaller impact.

*We agree that companies should provide detailed disclosures in relation to all material and other significant ESG related matters. These will be different for each industry, and may even be different for companies in the same industry based on many unique factors (company size, product mix, company lifecycle, regulatory and reporting framework, company strategy, etc.). It will often take engagement between issuers and investors and stakeholders to settle on which disclosures are most appropriate.*

**2.4 Financial and Non-Financial Impacts**

The NFRD requires companies to disclose “principal risks” in the non-financial statement, which may include the potential financial consequences of climate change. In comparison, a primary objective of the TCFD recommendations is to solicit information on climate-related financial impact.

*CFA Institute strongly supports the disclosure of all material ESG factors and encourages companies to adopt a recognized framework to enable investors and stakeholders alike to properly evaluate material ESG risks, including climate related risks.*

**2.6 Strategic Resilience and Scenario Analysis**

The TCFD also recommends companies disclose the resilience of their strategies. s. NFRD asks for information that is "necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, environmental, […] anti-corruption and bribery matters."

*CFA Institute agrees that scenario analysis is a useful tool that can be applied to help both issuers and investors better understand the potential implications of climate change and the resilience of companies to those implications ("strategic resilience").*

**2.7 Capturing Climate-related Opportunities**

The NFRD does not make explicit reference to opportunities but climate-related opportunities, such as those associated with "business relationships, products or services" with a climate mitigation or adaptation utility or investments in the development of solutions for moving toward a low-carbon and climate-resilient economy, can be considered risk mitigation measures. The TCFD encourages disclosure of both climate-related risks and opportunities.

*In our partnership with PRI aimed at better understanding the current state of ESG integration around the world, we observed that all markets we visited looked at ESG integration (including climate issues) primarily through a risk lens. However, those markets that had the most sophisticated approaches to ESG integration (climate issues included) tended to look for opportunities presented by ESG integration just as much as they focused on risk. The economics of climate change will present both risks and opportunities to companies and their investors.*

**3. Alignment of NFRD and TCFD**

The Task Force mapped the TCFD's recommended disclosures to the elements of the NFRD to inform the proposed climate-related reporting guidelines. The structure of the NFRD, which is made up of five elements (see Table 1), has been used to analyze how the TCFD's recommended disclosures support, specify, and streamline the implementation of the NFRD for a better understanding of a company's development, performance, position, and impact of its activities concerning climate-related issues.

Table 1 – NFRD Elements and TCFD Recommendations

| NFRD Elements (Broader Sustainability Approach) | TCFD Recommendations (Specific Climate Change Approach) |
|---|---|
| Business model | Governance |
| Policies and due diligence processes | Strategy |
| Outcomes | Risk Management |

| Principal risks and their management | Metrics and targets |
|---|---|
| Key performance indicators (KPIs) | |

The TCFD's four overarching recommendations are supported by eleven recommended disclosures that build out the framework with information that helps stakeholders understand how companies assess their climate-related risks and opportunities. Companies should determine the form and content of their reporting based on many factors, including their specific business model and approach to managing climate-related risks and opportunities.

The TCFD Recommended disclosures and their subcategories are listed below for reference.

Governance

- Board Oversight
- Management's role

Strategy

- Climate-related risks and opportunities
- Impact of climate-related risks and opportunities
- Resilience of the organization's strategy

Risk Management

- Processes for identifying and assessing
- Processes for managing
- Integration into overall risk management

Metrics & Targets

- Metrics used to assess
- GHG emissions
- Targets

To facilitate TCFD-aligned disclosure, the Task Force has mapped out the TCFD's eleven recommended disclosures to the five elements of the NFRD is showing companies and investors places of overlap that allows both parties a guide to help focus their attention. See figure 1

Figure 1

| | NFRD Elements | | | | |
|---|---|---|---|---|---|
| TCFD Recommended Disclosures | Business Model | Policies and Due Diligence Processes | Outcomes | Principal Risks and Their Management | Key Performance Indicators |

| | | | | | | |
|---|---|---|---|---|---|---|
| Governance | TCFD Recommended Disclosures | | x | | | |
| | Board Oversight<br>Management's Role | | x | | | |
| Strategy | Climate-related risks and opportunities | x | | | x | |
| | Impact of climate-related risks and opportunities | x | | x | | x |
| | Resilience of the organization's strategy | x | | x | x | |
| Risk Management | Processes for identifying and assessing | | x | | x | |
| | Processes for managing | | x | | x | |
| | Integration into overall risk management | | x | | x | |
| Metrics & Targets | Metrics used to assess | | | x | | x |
| | GHG emissions | | | | | x |
| | Targets | | | x | | x |

*This is a simplified version of graphic from the Technical Expert Group's report showing areas of overlap between TCFD Recommended Disclosures and NFRD Requirements. For a more detailed version of this graphic see The Task Force report itself.

*CFA Institute sees the mapping of TCFD recommended disclosures and elements of the NFRD as a sound starting point for investors wishing to incorporate climate related disclosures in their process of analysis.*

**4. Proposed Disclosures**

This section of the Technical Expert Group report focusses on the type and quality of climate-related disclosures that can be decision-useful for a company's stakeholders, addressing both the company's impacts on climate change and the potential financial impacts of physical climate-related risks and the transition to a low-carbon and climate-resilient economy on the company.

These proposed guidelines are based on certain disclosures on which a strong consensus has been reached among standard setters, while leaving companies free to go further. For each of the five NFRD elements, the guidelines describe: 1) rationale and context addressing the importance of reporting

the suggested information, 2) references to relevant TCFD recommended disclosures, and 3) specific proposed disclosures companies are encouraged to provide in their reporting.

There are three types of disclosures, which are signposted throughout the guidance by the use of the phrases "should / should disclose," "should consider / should consider disclosing" and "may consider / may consider disclosing," as follows:

- Type 1 disclosures – those that companies should disclose (high expectation that all reporting companies disclose them)

- Type 2 disclosures – those that companies should consider disclosing (expected of companies with significant exposure to climate-related risks and opportunities)

- Type 3 disclosures – those that companies may consider disclosing (additional or innovative disclosures that provide more enhanced information)

The "general disclosures" (Type 1) refer to information that companies should disclose. At a minimum, a company is expected to report certain disclosures, irrespective of the companies' own assessment. Additionally, companies should report a set of climate-related information according to the five NFRD disclosures elements as required by the NFRD, except if – based on the company's own assessment carried out autonomously and/ or in consultation with stakeholders – this information is regarded as unnecessary for an understanding of the company's development, performance, position and of its activities relating to climate change matters.

The "supplementary disclosures" (Type 2) refer to information that companies should consider reporting on and depend on the company's own assessment of impacts of climate change on its business.

*CFA Institute sees this Type 1, Type 2, and Type 3 model of disclosure with the TCFD and NFRD disclosure recommendations as a solid framework for issuers and investors to work with. This disclosure approach allows companies suitable flexibility around the climate related disclosures that are most relevant to them. This disclosure framework also allows issuers and investors to adjust the framework in a way that works best for them.*

### 4.1. Business Model

The NFRD requires companies to disclose "a brief description of the undertaking's business model." Stakeholders may be interested in understanding the company's view of how climate change might affect its business model, and how its activities might affect climate change, over the short, medium and long term.

Companies that do not appropriately consider their business model in light of climate change may both cause negative effects on the environment and experience negative impacts on their business such as on the profit and loss statement, debt financing, future regulatory burden, and "license to operate" in terms of reputational costs.

*CFA Institute believes that a discussion of a company's business model and how it is and is not impacted by climate change is a reasonable disclosure for investors and other stakeholders to expect from the companies in which they invest. As mentioned above, the scope of this disclosure and what it does and*

*does not include will depend on a company's sector and can be worked out through engagement between a company and their investors and stakeholders.*

#### 4.2. Policies and Due Diligence Processes

The NFRD requires companies to provide "a description of the policies pursued by the company in relation to those non-financial matters, including due diligence processes implemented."

Governance and control systems are key to stakeholders' understanding of the robustness of a company's approach to climate-related issues. Information on the involvement of board members and top management, in particular their respective responsibilities in relation to climate change, informs stakeholders on the level of the company's awareness of climate-related issues.

*CFA Institute feels that much of this disclosure around policies and due diligence processes should already be part of discussions between a company and their investors and stakeholders. Indeed, this process has already been undertaken by leaders in both the issuer and investor/stakeholder communities and can be looked at as examples by those issuers looking to improve their engagement and disclosure regimes.*

#### 4.3. Outcomes

The NFRD requires companies to disclose "the outcome of the company's policies."

Disclosure of policy outcomes helps providers of capital, as primary users of non-financial statements, and other stakeholders monitor and assess a company's development, position, performance and impact as a result of its policies.

*It may be difficult for many companies to satisfy the outcomes that the Technical Expert Group outlines in this report.*

*In some cases, companies may have a clear idea of the impacts their operations do and do not have on climate change. However, this area of reporting is very new to most companies, many of whom have not discussed these issues in the level of detail called for in this report at the board, management and operational level. Smaller companies may also lack the resources to track this data to the extent their larger competitors can, and to the extent outlines in this report.*

*It would therefore be helpful if the taskforce could offer further guidance in this area to companies. Many companies don't know "how" to report to the specificity that the Technical Expert Group speaks of in this report. Helping issuers with that knowledge and the resources they need to integrate that knowledge in their reporting would be helpful.*

#### 4.4. Principal Risks and Their Management

The NFRD requires companies to disclose "the principal risks related to those matters linked to the undertaking's operations including, where relevant and proportionate, its business relationships, products or services which are likely to cause adverse impacts in those areas, and how the undertaking manages those risks."

When a company has assessed specific climate-related risks (including transition risks and / or physical risks) and opportunities, it is important that stakeholders understand what those specific risks and opportunities are and how the company manages them. Stakeholders may be seeking information on the company's ability to manage its business if certain uncertainties materialize. Stakeholders may also want information on the company's impact on the climate, especially providers of financial capital interested in environmentally conscious companies.

*CFA Institute agrees that a primary focus of the Technical Expert Group's report should focus on risk assessment and risk management as we have seen this as a main driver of integration of ESG data in the investment process. Yet, climate change is often spoken of and written about with only an eye on the risk side of the equation. A recognition and greater focus on a company's climate change profile may also offer immense opportunities to find solutions.*

**4.5. Key Performance Indicators**

The NFRD requires companies to disclose "non-financial key performance indicators relevant to the particular business." Companies should use KPIs to support their other climate-related disclosures, such as those related to outcomes or principal risks and their management, and to connect qualitative disclosures with quantitative information.

As climate-related risks and opportunities are relevant for companies across all sectors, all companies should disclose - at a minimum - general, broadly recognized climate-related KPIs on current GHG emissions and GHG emissions targets.

*CFA Institute agrees that companies should disclose material key performance indicators related to all ESG issues including climate change KPIs. Several frameworks exist in this field including the TCFD, GRI, SASB approaches and we see these standards as a useful baseline for disclosure around ESG. We expect and encourage that issuers/ investors/stakeholders will continue work to improve these framworks.*

**Conclusion**

We thank the Technical Expert Group for the opportunity to comment on this matter and are happy to discuss this matter further if the European Commission wishes to do so. Should you have any questions about our positions, please do not hesitate to contact Jim Allen, U.S. Head of Capital Markets Advocacy, Washington D.C. at jim.allen@cfainstitute.org or 434-951-5558.

Sincerely,

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