CONSULTATION RESPONSE

BEIS: CONSULTATION ON REQUIRING MANDATORY CLIMATE-RELATED FINANCIAL DISCLOSURES BY PUBLICLY QUOTED COMPANIES, LARGE PRIVATE COMPANIES AND LLPS

May 2021

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THE PRINCIPLES FOR RESPONSIBLE INVESTMENT

The United Nations-supported Principles for Responsible Investment (PRI) is the world's leading initiative on responsible investment. The PRI has over 3,800 signatories (pension funds, insurers, investment managers and service providers) globally with approximately US $100 trillion in assets under management.[1]

The PRI works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society. The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

This consultation response represents the view of the PRI Association and not necessarily the views of its individual members. More information: www.unpri.org

ABOUT THIS CONSULTATION

Under this proposal, the Department for Business, Energy and Industrial Strategy would make it mandatory for Public Interest Entities (PIEs), UK registered companies with securities admitted to AIM and with more than 500 employees, and UK registered companies and LLPs which have more than 500 employees and turnover of more than £500m to disclose climate-related financial information in line with the 4 TCFD pillars of governance, strategy, risk management, and metrics and targets. These regulations would affect accounting periods beginning on or after 6 April 2022.

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[1] See https://www.unpri.org/signatories/signatory-resources/signatory-directory

SUMMARY OF THE PRI'S POSITION

The PRI welcomes BEIS proposals on enhancing climate-related reporting requirements. However, in their current form, they will fail to provide the comprehensive and comparable disclosures for market participants to adequately manage exposure to climate risk.

As hosts of COP26 and as home to one of the world's main financial centres, several other markets look to the UK's proposals to inform their own decision-making. Leadership on TCFD implementation by the UK would support increased global ambition on climate reporting.

The PRI recommends that BEIS:

- **Require mandatory disclosures for companies in line with the 11 recommendations of the TCFD**

The 11 recommendations of the TCFD are broadly well-understood and have become industry standard. Disclosure against the 4 pillars only does not adequately address a firms' risk management and strategy-setting processes and risks creating confusion for preparers. This would include a requirement to disclosure the resilience of the companies' business strategy to a range of climate-related scenarios. In addition, the consultation appears to propose a 'comply or explain' approach which is not only inconsistent with requirements for investors, but also raises the prospect that if companies fail to provide adequate disclosures there will be significant gaps and deficiencies in the data investors rely on to make prudent investment decisions and accurately fulfil their own disclosure requirements.

- **Extend the proposed scope of TCFD reporting to companies with 250 employees and/or a turnover of £36 million per annum.**

The scope of TCFD reporting should be extended to companies with over 250 employees or $36 million in revenue as per the reporting threshold in BEIS's Streamline Energy and Carbon Reporting (SECR) legislation. For smaller firms the reporting requirement could be phased in where necessary.

- **Require companies to disclose a strategy that is aligned with the government's commitment to achieve net zero by 2050 and the Paris Agreement.**

The UK has committed to reducing its emissions by 78% (compared to 1990 levels) by 2035[2]in progress towards the Paris Agreement. Therefore the needs of investors have evolved beyond just the climate-related risk exposures which the TCFD focuses on, and towards how companies are aligned with and contributing to the transition to a net zero economy, supported by a credible plan on how they will achieve this target. The Race to Zero campaign has seen over 1,100 companies commit to achieve net zero greenhouse gas emissions by 2050 at the latest, with many setting earlier targets.[3] TCFD is a necessary foundation to ensure granular and comparable disclosures to hold companies to account for such commitments, though further disclosures may be required.

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[2] https://www.gov.uk/government/news/uk-enshrines-new-target-in-law-to-slash-emissions-by-78-by-2035

[3] https://unfccc.int/news/commitments-to-net-zero-double-in-less-than-a-year

DETAILED RESPONSE

Q1. Do you agree with our proposed scope for companies and LLPs?

No. **The PRI recommends extending the proposed scope of TCFD reporting to companies with 250 employees and / or a turnover of £36million per annum.** This scope would be in line with BEIS' Streamlined Energy and Carbon Reporting (SECR) legislation.

The UK Prudential Regulatory Authority notes "smaller firms are not immune from climate-related financial risk and could be more susceptible if they are particularly concentrated in a vulnerable sector, product or geography. Therefore, an appropriate approach depends on the firm's business model." Climate change poses risks to companies beyond the scope of those proposed for inclusion in this consultation and therefore as such, with respect to scope of companies for inclusion, disclosure requirements should likewise apply. BEIS could look to phase-in the new reporting requirements for companies under 500 employees over a multiyear period so as to avoid the new regulation disproportionally impacting smaller firms in the initial phase.

We note developments by the European Commission to adopt the Corporate Sustainability Reporting Directive (CSRD) which makes TCFD reporting mandatory. The CSRD expands the scope of companies reporting sustainability information from public interest entities to all large companies, all companies listed on EU regulated markets and the EU subsidiaries of non-EU companies (except listed micro-companies) following their findings that many stakeholders are in favour of extending reporting requirements to additional categories of companies.

Q4. Do you agree that the Strategic Report is the best place for the disclosure of climate-related financial information by companies?

Yes. **The PRI supports the inclusion of TCFD-aligned disclosures in the Strategic Report for large companies.** Historically, investors could find information on climate risk and opportunity in the Strategic Report, to allow information users to connect financial and climate-related financial information to develop a holistic overview of a company's risks and impacts and upholding this consistency would be vital in maintaining sustainability reporting which is comparable across firms, industries or markets.

Q6. Do you agree that requiring disclosure in line with the four pillars of the TCFD recommendations, rather than at the 11-recommendation level is suitable?

No. **The PRI recommend BEIS require disclosure in line with the 11 recommendations of the TCFD.** The current proposal only encompasses 8 of the 11 recommendations. The recommendations not currently included in the proposal are:

- *Strategy (c) scenario analysis;* the current proposal encourages but does not mandate the inclusion of scenario analysis. We would recommend mandating scenario analysis; please see our response to question 8 for more.
- *Risk (a) identifying and assessing climate-related risk;* a thorough and robust risk management system will have processes in place to identify and assess climate-related risk. It is not enough to simply state the risks. Investors should be informed as to how a firm identifies and assesses climate-related risk in order to form a comprehensive view of their climate risk management.

- *Risk (c) disclosing how climate risk management processes are integrated into overall organisation risk management*; Building on Risk (a), it is imperative that climate risk and opportunity is embedded into an overall firm strategy, rather than being relegated to one part of an organisation.

The 11 recommendations of the TCFD are broadly well-understood and have become industry standard. There has been significant growth in the number of investors reporting against the TCFD recommendations who are dependent on adequate climate disclosure. Among PRI signatories there has been a 350% increase in TCFD-based investor reporting in the first quarter of 2020, with 2,097 investors (443 asset owners, 1,654 asset managers) representing $89 trillion in assets reporting, compared with 591 investors the previous year. 330 of these investors were based in the UK – the second largest market by number of investors.[4] An additional 700 PRI signatories were under a reporting grace period as of this year but will report in 2021. These numbers will continue to grow. Disclosure against the 4 pillars only does not adequately address a firms' risk management and strategy-setting processes and risks creating confusion for both preparers and users.

Q7. Do you agree that information provided in line with the obligations set out above would provide investors, regulators and other stakeholders with sufficient information to assess the climate-related risks and opportunities facing a company or financial institution?

No. **The PRI recommends that BEIS require companies to disclose a strategy that is aligned with the goals of the Paris Agreement.**

Since the TCFD recommendations were formulated, several the world's largest economies have committed to achieve net zero greenhouse gas emissions by 2050 or sooner. The UK, in working to achieve this goal, has committed to reducing its emissions by 78% (compared to 1990 levels) by 2035.[5]The information needs of investors have therefore evolved beyond the climate-related risk exposures only, which the TCFD focuses on, to how companies are aligned with and contributing to the transition to a net zero economy.[6]

Encouraging companies to devise and disclose a strategy to achieve net zero emissions by 2050 is a key objective of Climate Action 100+, an initiative of over 450 investors engaging with over 160 of the world's highest emitting companies.[7] While an increasing number of companies have voluntarily disclosed high-level commitments to achieve net zero emissions by 2050, and in absence of a regulated requirement to do so, there is variance in the detail underpinning those commitments, and few companies have set out how their will practical implementation will support their commitments. Therefore, BEIS should require companies to disclose a strategy that is aligned with the government's commitment to achieve net-zero by 2050 and a credible transition plan with interim milestones and targets for achieving this goal. Disclosures on targets should include:

- The baseline year

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[4] https://www.unpri.org/climate-change/pri-climate-snapshot-2020/6080.article

[5] https://www.gov.uk/government/news/uk-enshrines-new-target-in-law-to-slash-emissions-by-78-by-2035

[6] https://www.responsible-investor.com/articles/with-the-tcfd-in-its-fifth-year-it-s-time-to-make-net-zero-mandatory-for-financialinstitutions

[7] https://www.climateaction100.org/news/climate-action-100-investors-seek-net-zero-business-strategies-through-company-engagement/

- Absolute emission reductions
- GHG emission intensity planned in five and ten years
- The level of coverage in company emission reporting. In line with CA 100+ benchmark PRI recommends at least 95% of scope 1 & 2 and the most relevant scope 3 emissions
- The methodology used to report scope 3 emissions and targets
- Interim targets for 2025, 2030 and 2035
- The degree of alignment including capital expenditure, with emission reduction targets

Q8. Do you agree with our proposal that scenario analysis will not be required within a company or LLP's annual report and accounts?

No. Testing the resilience of the business strategy against a range of future climate scenarios is at the heart of the TCFD recommendations and essential for companies to think forward on climate-related issues.

Whilst this exercise can be dauting for companies that need to undertake this for the first time, the level of complexity involves varies considerably. At the lower end of the scale, scenario analysis can be as simple as a firm explaining in qualitative terms what a net zero emissions target would mean for its business. At the higher end of the scale, it can involve quantitative modelling, based on a range of scenarios and linked variables over a range of different timescales.

As the TCFD Taskforce has highlighted there is a growing list of tools and resources available to companies on climate scenario analysis.[8] PRI supports the free-to-use Transition Pathway Initiative which provides analysis and an analytical framework for companies' management of climate-related issues and their carbon performance.

[8] See the Task Force on Climate-related Financial Disclosures Guidance on Scenario Analysis for Non-Financial Companies pp. 87-106.