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5 May, 2021

The Rt. Hon. Anne-Marie Trevelyan MP
Minister of State for Business and Clean Growth & UK International Champion on Adaptation and Resilience for the COP26 Presidency

Submitted by E-mail to: climatedisclosure@beis.gov.uk

Dear Ms. Trevelyan,

**CFA UK response to BEIS on their consultation on requiring mandatory climate-related financial disclosures by publicly-quoted companies, large private companies and Limited Liability Partnerships ("LLPs")**

The CFA Society of the UK (CFA UK) welcomes the opportunity to support the proposals in this consultation (the "Consultation"). CFA UK has consistently encouraged policy-makers to put in place a harmonised regime of climate-change disclosure obligations for all companies of a certain size, regardless of their ownership[1] [2].

CFA UK has also consistently advocated in favour of a speedy adoption of TCFD as the acknowledged global leading model for climate-related corporate reporting. CFA UK's mission is to help build a better investor profession for the ultimate benefit of society[3]. Helping our members to properly assess climate-related risks and opportunities in their investments, and so allocate capital correctly, is core to our purpose and behind our recent launch of the certificate in ESG investment and current development of a certificate in climate change investment [4] [5].

Our responses to the specific questions of the Consultation are provided in Appendix II. Should you have any questions or points of clarification regarding this letter, please contact Andrew Burton (aburton@cfauk.org) in the first instance.

Yours sincerely,

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Chief Executive
CFA Society of the UK

Andrew Burton
Professionalism Adviser
CFA Society of the UK

With thanks for the oversight of CFA UK's Professionalism Steering Committee

[1] *CFA UK Response to CP20/3 regarding Question 1 Scope (https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/ccdr-final-letter-to-fca.pdf)*

2 *CFA UK response to PS20/17 regarding Question 1 Scope (https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/ccdr-follow-up-letter-to-fca---february-2021.pdf)*

3 *A brief overview of both CFA UK and CFA Institute is provided in Appendix 1.*

4 *CFA UK Certificate in ESG Investing: (https://www.cfauk.org/study/esg#gsc.tab=0)*

5 *CFA UK Certificate in Climate Investing: (https://www.cfauk.org/study/climate-and-investing#gsc.tab=0)*

**Appendix I: About CFA UK & the CFA Institute**

**CFA UK:** serves nearly 12,000 leading members of the UK investment profession. Many of our members work with pension funds, either managing investment portfolios, advising on investments or as an in-house employee responsible for pension investment oversight.

- The mission of CFA UK is to build a better investment profession and to do this through the promotion of the highest standards of ethics, education and professional excellence in order to serve society's best interests.
- Founded in 1955, CFA UK is one of the largest member societies of CFA Institute (see below) and provides continuing education, advocacy, information and career support on behalf of its members.
- Most CFA UK members have earned the Chartered Financial Analyst® (CFA®) designation, or are candidates registered in CFA Institute's CFA Program. Both members and candidates attest to adhere to CFA Institute's Code of Ethics and Standards of Professional Conduct.

**CFA Institute:** is the global association for investment professionals that sets the standard for professional excellence and credentials.

- The organization is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Our aim is to create an environment where investors' interests come first, markets function at their best, and economies grow.
- It awards the Chartered Financial Analyst® (CFA), and Certificate in Investment Performance Measurement® (CIPM) designations worldwide; publishes research; conducts professional development programs; and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry.
- CFA Institute has members in 162 markets, of which more than 170,000 hold the Chartered Financial Analyst® (CFA) designation. CFA Institute has nine offices worldwide and there are 158 local member societies.
- For more information, visit www.cfainstitute.org or follow us on Twitter at @CFAInstitute and on Facebook.com/CFAInstitute.

**Appendix II: Responses to questions**

**Scope**

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

Yes.

As stated in our covering letter and previous consultation response letters sent to the FCA, we believe that collectively policymakers should seek to set the minimum bar for compliance with climate change disclosure requirements at the same level for all commercial and not-for-profit companies.

Specifically, CFA UK does not wish to encourage companies to go private, or to avoid listing, or adopt some other ownership structure to avoid obligations like reporting under TCFD. Also, whether a company is listed, private or set up as a limited partnership is of no direct consequence to either its carbon footprint or its vulnerability to climate change. Many of our members invest in private equity and would welcome these disclosures, not least because public IPO is a key exit-option for many private equity investments.

Additionally, we would underline that, from an investment context, many climate change related risks cannot be diversified away and so become a systemic consideration applying to all companies. Hence, CFA UK believe that all companies should bear the responsibility of recording their contribution and vulnerability to those risks – subject to them meeting a minimum size threshold.

In terms of the threshold itself, we agree reporting should be proportionate and concentrate initially on those companies which have (i) sizable operations which make their carbon footprint a matter of public interest and (ii) the ability and resources to be able to comply with the requirement.

However, we do not support a single-metric test for several reasons:

- it may be too easily circumvented. For example, a pure employee test can be circumvented by the outsourcing of certain activities to reduce employee headcount below the reporting threshold;
- nowadays, with the opportunity to rapidly scale a business digitally, there is a wider range of business models than ever before. Some companies that might be considered large, or of public interest, may be actually employing few staff;
- we note the established precedents in the Companies Act 2006 for using an "any-two-from-three" metric to define both small (S.382 – <50 employees, <£10.2m turnover, <£5.1m balance sheet) and medium sized (S.465 – <250 employees, <£36m turnover, <£18m balance sheet) companies. It would therefore seem appropriate and logical for a large company (that had to comply with TCFD reporting requirements) to be defined in a consistent way.

CFA UK notes that the definition of PIE is currently under consultation in the BEIS Restoring Trust in Audit and Corporate Governance paper[6]. We plan to address this question more fully in our response to that consultation.

[6] *Restoring trust in audit and corporate governance, Chapter 1 (https://www.gov.uk/government/consultations/restoring-trust-in-audit-and-corporate-governance-proposals-on-reforms)*

***Q2:* Our proposed scope includes UK registered companies with securities admitted to AIM with more than 500 employees. Do you have any views on expanding this to include other unregulated markets and Multilateral Trading Facilities (MTFs)?**

Since the proposals capture all companies of a certain size (minimum of 500 employees and £500 million turnover) that are not listed on AIM or a recognised exchange, this additional extension would seem to be unnecessary. It is important for our members involved in fixed income and credit markets that unlisted companies above a certain size are required to report their climate-related disclosures as their bond securities and loans are also often unlisted. However, we believe your other proposals on scope would address this point.

***Q3:* Do you agree with the proposal to require climate related financial disclosures for companies and LLPs at the group level?**

At the UK group company level, yes. Disclosure at a sole legal entity level would allow relevant disclosures in sister companies to be overlooked in the absence of a clear consolidated picture.

The directors at both the group company and material subsidiaries should be held responsible for the adequacy of the disclosures in instances where the disclosures relate to activities taking place within operating subsidiaries rather than at a group holding company.

CFA UK notes that this proposed legislation could affect overseas based companies with a relevant listing in the UK, overseas companies with UK subsidiaries and UK companies with overseas subsidiaries and so it makes sense for any regulations or legislation in this area to be harmonised internationally as much as possible.

In the advent of a carbon-tax in future years this may need to be revisited as corporation tax clearly functions at the sole legal entity level.

**Proposed Obligations**

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

Yes.

That said it is of critical importance that climate-related disclosures also are fully and properly considered in the financial statements in the valuation and impairment of assets and decisions around asset lives, stranded assets etc. The TCFD disclosures in the Strategic Report should reflect and connect with the numbers reported in the Financial Statements.

CFA UK notes that the question of the location of climate-related disclosures is also part of the more detailed BEIS consultation[7] which we plan to respond to by next month's deadline. Where such disclosures are an existential consideration for the company key points should also feature in the relevant section of the proposed resilience statement.

[7] *See footnote 4*

***Q5: Do you have views on whether LLPs should be required to disclose climate-related financial information in the Strategic Report (where applicable), or the Energy and Carbon Report?***

We believe a consistent approach should be adopted by all LLPs. Our preference would be that it was the same as for companies and in the Strategic Report, but this is not critical.

***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?***

As laid out in our response to question 1 above, we believe all companies should be subject to equal treatment, regardless of their ownership structure and proportionate to their size.

We note that under PS20/17 the FCA will now require premium listed companies to report at the 11 recommendation level but on a comply-or-explain basis.

In our responses to the FCA (referred to previously) with regards to their question 4 we opined that not all of the 11 recommendations should be comply-or-explain and that 5 should be mandatory. Specifically, these are: i) Governance a), ii) Strategy a), iii) & iv) Risk Management a) & b) and v) Metrics & Targets a). We believe companies should be able to articulate the way they now perceive climate-change may impact their business and its markets in the future and, as a consequence, how they are beginning to govern, form strategy, risk manage and measure this.

We therefore fully support BEIS' proposal here that companies are required to report against these same 5 recommendations (the first two in Risk Management and just the first in the other three categories), not through new but through existing statutory powers under the 2006 Companies Act.

We will hope and expect to see more companies reporting under full compliance with all 11 recommendations in the relatively short-term such that in a few years the other 6 recommendations will over time also become mandatory.

***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?***

Responding on behalf of our members who are investors - no.

The information to be provided in the Consultation's proposals represents a considerable step forward from current requirements and the fact that it is now mandatory means that analysts should start to see information with less positive bias (i.e. corporates reporting at length on positive impacts and glossing over or ignoring the downsides).

That our members support only these 5 recommendations become a mandatory requirement today is an acknowledgement of the practical reality: namely, that companies are only at the relative beginning of being able to quantify and assess the risks and opportunities that climate change may represent to them. Whilst some companies are already voluntarily reporting in full compliance with TCFD requirements, the vast majority are a long way from being capable of doing that even if they wanted to. The proposal also reflects the reality that most companies must start to seriously consider this issue now if they have not already.

These proposals therefore only provide a baseline for what companies should be required to provide. They do not provide investors with sufficient information to fully assess the climate related risks that companies face. In summary, the proposed requirements should provide some indication of the risks faced and, perhaps more importantly, how seriously each company is beginning to consider them currently.

We believe it is relevant to highlight a report published last year by CFA Institute[8]. The second half of this publication is devoted to a dozen 'real-life' case studies. These provide additional colour as to the type of information investors are looking for to be disclosed by investees and how it can be used not just in analysing equity investments but across a range of other asset classes. It is also instructive to read that BEFORE 2030 on a 2°C scenario, climate change is anticipated to present transformational investment opportunities and risks across the utility, real estate, cement, oil and gas, aerospace, food and consumer goods, automotive, semiconductor and electrical equipment, agriculture, chemical and construction sectors.

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

CFA UK notes that in Chapter 3 of their Consultation on Restoring Trust in audit and governance[9] BEIS proposes companies must include at least two reverse stress tests within the medium- to long-term section of their resilience statement. For some companies it is highly likely that one, or both, of these stress tests will contain climate-driven assumptions.

As investors, we derive great value from stress tests, their outputs and the sensitivities that they reveal. At this stage, we are content to see the inclusion of climate-related scenarios and stress tests encouraged and included in the annual report as best practice. Where they are not included in the report, they should ideally be referenced to a web-page. We would also be keen to encourage qualitative (as opposed to quantitative) scenario analysis where insufficient (or insufficiently reliable) figures are only available – which is the case currently in many cases.

***Q9: Would alignment of the scope for climate-related financial disclosures and SECR requirements, such that large unquoted companies and LLPs would be subject to the same reporting requirements under SECR as quoted companies, aid reporting of climate related financial disclosures and simplify reporting procedures? Do you have any views on the continuation of voluntary Scope 3 emissions reporting under SECR requirements?***

Yes. CFA UK would support alignment and consistency of treatment.

CFA UK would regard the continuation of voluntary Scope 3 emissions targets as best practice.

***Q10: Do you have comments on the proposal to permit non-disclosure if the information is not material and the reasons why climate change is not material are properly explained?***

[8] *"Climate Change Analysis & the investment process" (https://www.cfainstitute.org/en/research/industry-research/climate-change-analysis)*
[9] *See footnote 4*

As we responded to the FCA in our response to question 8, we believe all in scope companies should be required to provide climate-related disclosures. If a company believes that climate considerations are non-material then they may state the reason for this and investors can come to their own conclusions. Non-disclosure on the grounds of immateriality should not be permitted.

**Timing**

***Q11: Do you have comments on the proposed timing for these regulations coming in to force?***

The timings seem reasonable. CFA UK note that these proposals allow for a longer lead-in time than the FCA requirements for premium listed companies which were announced in PS20/17 in late December 2020 to take effect on companies from their next financial year-end commencing after 1st January 2021.

**Enforcement, Penalties & Timing**

***Q12: Do you have any comments regarding the existing enforcement provisions for companies and the BEIS proposal not to impose further provisions?***

No comments.

***Q13: Do you have any comments regarding duties and enforcement provisions for LLPs?***

No comments.

**Auditors**

***Q14: Do you have any comments on the responsibilities of auditors in relation to climate-related financial disclosures?***

In situations where auditors consider climate related risks (or opportunities) to be critical for the company they are auditing, auditors (and investors) they should have the ability, to formally request that the company appoint a specialist climate consultancy firm to provide independent expert opinion. If such a request is refused, then that should be noted in the auditor's opinion. We encourage more auditors to include climate change considerations within their audit report disclosures, and to use climate change and carbon market experts to help deliver effective audits.

CFA UK remains of the view that it is too early to make assurance mandatory on TCFD reporting and that currently to insist on auditor assurance would be a retrograde step. Whilst we anticipate significant progress in this area over the next few years, at present the numbers of companies embracing TCFD reporting, the adequacy of both reporting and auditing infrastructures is insufficiently developed to make mandatory assurance sensible. We note that again this issue of the broader assurance role of the audit profession is considered in the Restoring Trust in Audit and Corporate Governance consultation, and we will make comments on this in our response to that.

***Q15*: *Do you have any comments regarding the proposed enforcement of our disclosure requirements?***

As stated previously in our response to question 6, we believe that differential treatment for companies under different ownership is unfair and could be a source of unnecessary confusion and would prefer that requirements were harmonised for all in-scope companies as far as possible. In so far as these reporting regimes are or must remain different, then we concur that the FRC and the FCA must operate a consistent approach to monitoring and enforcement of these requirements.