CDP and CDSB response to HM Treasury's inquiry on Decarbonisation of the UK Economy and Green Finance

CDP and the Climate Disclosure Standards Board (CDSB) welcome the opportunity to offer our written submission to the Treasury's inquiry on Decarbonisation of the UK Economy and Green Finance published in June 2019.

CDP is a global environmental impact non-profit working to secure a thriving economy that works for people and planet. High quality, relevant information is the fundamental basis for action and CDP helps investors, companies and cities to measure, understand and address their environmental impact. The world's economy looks to CDP as the gold standard of environmental reporting with the richest and most comprehensive dataset on corporate and city action. CDP aims to make environmental reporting mainstream and provide the detailed insights and analysis to drive the urgent action needed for a climate safe, water secure, deforestation free world. CDP recognises the important role of the Task Force on Climate-related Financial Disclosures (TCFD) in mainstreaming climate-related information and advancing the availability of financially relevant information for global markets. Therefore, CDP has aligned its information requests with the TCFD recommendations, alongside introducing a sectoral focus and adopting a forward-looking approach to climate risk disclosure.

CDSB is an international consortium of nine business and environmental NGOs. We are committed to advancing and aligning the global mainstream corporate reporting model to equate natural capital with financial capital. We do this by offering companies a framework for reporting environmental and climate information (the CDSB Framework) with the same rigour as financial information. In turn, this helps companies to provide investors with decision-useful environmental and climate information via the mainstream corporate report, enhancing the efficient allocation of capital. Regulators also benefit from compliance-ready materials. Recognising that information about natural capital and financial capital is equally essential for an understanding of corporate performance, our work builds the trust and transparency needed to foster resilient capital markets.

Collectively, CDP and CDSB aim to contribute to more sustainable economic, social and environmental systems. CDP and CDSB are also members of the UK's Green Finance Initiative (GFI) working group on Data, Disclosure and Risk and work closely with HM Government on a range of issues to support the advancement of the UK's sustainable finance initiatives.

Our responses to specific questions are in Annex I below. Please do not hesitate to get in touch in case we can be of further assistance.

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Appendix I: Responses to consultation questions

The economic opportunity:

1. What economic costs and benefits does decarbonisation present for the UK?

As highlighted in the UK's Green Finance Strategy, 2017 was the costliest year for insurers for weather disasters at $132 billion[1]. On the other hand, the report also notes the significant opportunity associated with addressing climate change, noting that "With a leading financial services sector, the UK is ideally placed to seize the commercial potential arising from this transition"[2].

A group of the world's largest companies representing nearly US$17 trillion in market capitalization have valued the climate risks to their businesses at almost US$1 trillion - with many likely to hit within the next 5 years. This is evidenced by new a new report by CDP, analysing corporate CDP responses. The key findings from this report are listed below, and clearly show there is an economic imperative to act on climate change and decarbonise:

a. The 215 biggest global companies report almost US$1 trillion at risk from climate impacts, with many likely to hit within the next 5 years;
b. Companies report potential US$250 billion in losses due to the write-offs of assets;
c. Climate business opportunities calculated at US$2.1 trillion, nearly all of which are highly likely or virtually certain;
d. Potential value of sustainable business opportunities almost 7x the cost of realizing them (US$311bn in costs, US$2.1 trillion in opportunities);
e. Financial companies forecast US$1.2 trillion in potential revenue from low emissions products & services; and
f. Financial services industry represents almost 80% of the total potential financial impacts in the sample set.

2. What benefits can a growth of the Green Finance sector deliver for the UK, and does the UK hold a competitive advantage in this space?

The finance sector can avoid significant losses by managing climate risk proactively, thus better protecting the savings and investments of individuals in the UK, as well as positioning the UK's finance sector as a resilient financial centre globally.

According to CDP's latest research, 80% of companies operating in the financial services, fossil fuels, and power industries identify substantive climate-related risks and opportunities – the highest proportion in comparison to other industries.[3] Given the significant changes taking place in the energy sector as a result of climate-related policies, market dynamics, and technology shifts, it is unsurprising to see this level of substantive impact identified in fossil fuel and power companies. At the same time, the finance sector is providing capital to these sectors and experiencing an increasing focus on climate-related risks, brought to light among others through the work of the Bank of England's Prudential Regulatory Authority[4], the TCFD, as well as other central banks, supervisors, and financial regulators globally.

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[1] Reuters (retrieved June 2019) 2017 second-costliest year on record for natural-disaster insured losses: Aon. [Online]. Available from: https://www.reuters.com/article/us-global-insurance-aon/2017-second-costliestyear-on-record-for-natural-disaster-insured-losses-aon-idUSKBN1FD22Y

[2] HM Government (2019) Green Finance Strategy. [PDF]. Available from: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/820284/190716_BEIS_Green_Finance_Strategy_Accessible_Final.pdf

[3] The analysis is based on the world's 500 biggest companies by market cap (G500), 366 of whom reported to CDP in 2018.

[4] See for example:
Prudential Regulator Authority (2015) The impact of climate change on the UK insurance sector. [PDF]. Available from: https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/publication/impact-of-climate-change-on-the-uk-insurance-sector.pdf?la=en&hash=EF9FE0FF9AEC940A2BA722324902FFBA49A5A29A; or

The majority of financial implications reported to CDP are concentrated in the financial services industry – they are the biggest sector represented in the G500 (the 500 largest companies globally) and they are disclosing these risks more readily than others. On the other hand, over half of the total financial value from increasing opportunities is also identified by the finance sector, where reported opportunities total over US$1.2 trillion.[5]

Green Finance:

10. Are there any barriers (regulatory or otherwise) preventing financial services firms from delivering green finance or investing in 'green' assets?

Yes. While we would welcome the opportunity to discuss the specifics, in general the regulatory and wider landscape does not incentivise financial services firms to create green financial products or invest in green assets. In addition, there is a lack of clarity and rigour in defining 'green' assets in the first place, as it is not codified within the UK's regulatory framework, leaving it open to interpretation.

To mainstream and normalise sustainable investment, which provides financial, environmental and social returns, and to avoid global financial stability risk from mispriced unsustainable investments, governments, central banks, investors, banks and companies must work together to promote trustful and efficient capital allocation decisions based on prudent and proactive climate-related financial disclosures.

Disclosure is the bedrock of mainstreaming sustainable finance. Multi-annual global corporate environmental data, aligned with the recommendations of the Taskforce on Climate-related Financial Disclosures enables public and private investors to incorporate climate-related risks and opportunities in their decision-making process, and to benchmark their alignment with the goals of the Paris Agreement. Financial regulators can also address the financing of the related shifts in the structure of the economy and the investments required to adapt to climate change, as well as monitor potential macroprudential risks associated with climate change. More information on possible avenues for inclusion of the TCFD recommendations into national legislation in G7 jurisdictions can be found in CDP and CDSB's Roadmap for Adopting the TCFD recommendations.

11. What prudential risks does climate change pose?

Climate change not only has the potential to result in losses in the magnitude of trillions of dollars[6], but an abrupt and disorderly transition would also damage the economy – coined as a *Climate Minsky Moment* by Bank of England Governor Mark Carney. Indeed, too rapid a shift could materially damage financial stability, as massive reassessments of assets destabilize markets, spark losses and lead to a tightening of financial conditions.

With 2017 and 2018 seeing significant losses from extreme weather incidents in parts of the world, as well as rapid technological shifts taking place in certain sectors as a result of the transition towards a low-carbon economy, financial regulators and investors are becoming increasingly focused on ensuring the private sector is ready for the risks and opportunities of climate change.

Prudential Regulator Authority (2018) Transition in thinking: The impact of climate change on the UK banking sector. [PDF]. Available from: https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/report/transition-in-thinking-the-impact-of-climate-change-on-the-uk-banking-sector.pdf?la=en&hash=A0C99529978C94AC8E1C6B4CE1EECD8C05CBF40D

[5] The response to question 2 is adapted from CDP's 2019 report *"Major risk or rosy opportunity – Are companies ready for climate change?"* p.6: https://www.cdp.net/en/research/global-reports/global-climate-change-report-2018/climate-report-risks-and-opportunities

[6] The estimated losses are large – $1tn-$4tn when considering fossil fuels alone, or up to $20tn when looking at a broader range of sectors according to the Network of Central Banks and Supervisors for Greening the Financial System (NGFS). Available from: https://www.banque-france.fr/sites/default/files/media/2019/04/17/ngfs_first_comprehensive_report_-_17042019_0.pdf

12. What is the Financial Conduct Authority and the Prudential Regulation Authority doing to support decarbonisation and a 'greening' of the financial system?

The HM Green Finance Strategy provides a comprehensive list of activities undertaken by the FCA and PRA to support green finance in the UK.[7]

Among other activities, the FCA and PRA have formed the Climate Financial Risk Forum, which was set up to build capacity and share best practice across financial regulators and industry to advance financial sector responses to the financial risks from climate change. It brings together senior representatives from across the financial sector, including banks, insurers, and asset managers. This approach of collaboration with the market on the voluntary level, combined with mandatory measures where necessary, are key to incentivising the decarbonisation and greening of the financial system.

(b) What expectations do (and should) they place on regulated firms about their role in the transition through their policy and supervisory activities?

It is crucial for the FCA and PRA to take into account latest scientific evidence from the United Nations Framework Convention on Climate Change (UNFCCC), as well as reports published by the PRA, the Network of Central Banks and Supervisors for Greening the Financial System (NGFS) and many others to create an environment where the risks and opportunities associated with a low carbon, sustainable financial system are front of mind and taken into account by the market.

15. Do accompanying documents for 'green' instruments (bonds, funds, etc) articulate why and how the composite holdings within that instrument are 'green'? Are obligations placed upon listed companies, to report their carbon emissions, to inform fund composition?

CDSB and CDP's review of corporate reporting in Europe[8] has shown that while the UK is ahead of the pack in corporate reporting of climate change- and natural capital-related information, there is still a gap in the reporting of the impact of such matters on the business. Policy instruments, such as the 2013[9] and 2017[10] amendments to the Companies Act 2006 do not yet go far enough to specify climate-related financial reporting requirements, as defined for example by the recommendations of the G20 Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD).

In the Green Finance Strategy, HM Government has set an expectation for all listed companies and large asset owners to disclose in line with the TCFD recommendations by 2022, while simultaneously establishing a joint taskforce with UK regulators, chaired by Government, which will examine the most effective way to approach disclosure, including exploring the appropriateness of mandatory reporting.

It is important to monitor progress on TCFD adoption closely in order to ensure that information is reported by companies to their investors. Such information is the basis on which investors can articulate the 'greenness' holdings and portfolios more broadly. CDSB and CDP would like to offer its support to HM Government with this monitoring effort, based on a combined 30+ years of monitoring corporate reporting on a global scale.

[7] See for example pp 20-21. HM Government (2019) Green Finance Strategy. [PDF]. Available from: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/820284/190716_BEIS_Green_Finance_Strategy_Accessible_Final.pdf
[8] CDSB & CDP (2018) First steps: Corporate climate and environmental disclosure under the EU Non-Financial Reporting Directive. [PDF]. Available from: https://www.cdsb.net/first-steps-corporate-climate-environmental-disclosure-under-eu-non-financial-reporting-directive
[9] Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013
[10] Companies, Partnerships and Groups (Accounts and non-financial reporting) Regulations 2016