

# **Enhancing climate-related disclosures by standard listed companies and seeking views on ESG topics in capital markets**

**Consultation Paper**

CP21/18\*\*

June 2021

## How to respond

We are asking for comments on this Consultation Paper (CP) by **10 September 2021**.

You can send them to us using the form on our website at: [www.fca.org.uk/cp21-18-response-form](http://www.fca.org.uk/cp21-18-response-form)

Or in writing to:

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# 1 Summary

## Why we are consulting

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- 1.1** Effective capital markets rely on good corporate disclosures to inform asset pricing and capital allocation. Climate change is a relevant consideration for all companies and likely to be material for most.
- 1.2** In this consultation paper (CP) we propose extending the application of our climate-related disclosure requirements for commercial companies with a UK premium listing to issuers of standard listed equity shares (excluding standard listed investment entities and shell companies). These disclosure requirements reference the recommendations published by the Financial Stability Board's (FSB) Taskforce on Climate-related Financial Disclosures (TCFD) in 2017.
- 1.3** We are consulting at the same time, in a separate consultation paper, [CP 21/17](#), on proposals to introduce climate-related disclosure requirements for asset managers, life insurers, and FCA-regulated pension providers. These would also align with the TCFD's recommendations.
- 1.4** The physical risks of climate change – including the increased frequency of extreme weather events – can affect companies' operations, their supply chains and financial commitments such as insurance costs. Equally, transition risks arise as companies adjust to the inevitable strategic, regulatory and economic implications of the transition to net zero carbon emissions. Of course, for some companies, this transition may also present opportunities. Those that embrace change and develop and deliver products that align with a net zero future may thrive.
- 1.5** The current quantity and quality of climate-related financial disclosures does not yet meet investors' needs. That's why one of our key priorities has been to enhance climate-related disclosures along the investment chain, beginning with listed companies.
- 1.6** The TCFD's recommendations provide the leading framework for climate-related financial disclosures. In November 2020, the Government published a [Roadmap](#) charting a path towards mandatory TCFD-aligned disclosure obligations across the UK economy over the next five years. Most of the measures are expected to be introduced by 2023.
- 1.7** We took our first step in December 2020, implementing a new disclosure rule for commercial companies with a UK premium listing, referencing the TCFD's recommendations. Our rule was finalised in [PS20/17](#), following a consultation process during 2020 ([CP20/3](#)). The measures we propose in this CP extend the application of the requirements for premium listed companies to a wider scope of issuers, consistent with our commitments in the Roadmap.

- 1.8** In addition to the measures we are taking, the Government Department for Business, Energy and Industrial Strategy (BEIS) recently conducted a consultation on climate-related disclosure provisions in the Companies Act 2006 and Limited Liability Partnerships Act 2000. The Department for Work and Pensions (DWP) has also published draft regulations for trustees of occupational pension schemes.
- 1.9** We have also included a discussion component in this CP (see Chapter 4). We aren't proposing rule changes but instead are asking for views on select Environmental, Social and Governance (ESG) topics in capital markets. We are specifically looking to generate discussion and engage stakeholders on i) issues related to green, social or sustainable debt instruments and ii) ESG data and rating providers.
- 1.10** These are active areas of industry debate and therefore we are looking to gather views on potential harms that may need further policy intervention.

## Who this applies to

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- 1.11** Our proposals will directly affect issuers of standard listed equity shares (excluding standard listed investment entities and shell companies) and may also impact issuers of standard listed shares other than equity shares, issuers of standard listed debt (and debt-like) securities and issuers of standard listed global depositary receipts (GDRs). We also note that some of the proposals in this CP may impact premium listed commercial companies who are in-scope of our existing LR 9.8.6R(8).
- 1.12** Our consultation paper and discussion chapter will also interest a wide range of stakeholders, including:
- corporate finance and other advisers
  - consumer groups and individual consumers
  - investors and asset owners
  - sponsors of listed companies
  - accountants, auditors and second party opinion providers
  - ESG data and rating providers
  - industry groups, trade associations and civil society groups
  - regulated firms
  - policymakers and regulatory bodies
  - industry experts and commentators
  - academics and think tanks

## What we want to change

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- 1.13** Building on our requirements for premium listed commercial companies, we are now proposing to apply TCFD-aligned disclosure requirements to a wider scope of commercial companies – bringing into scope issuers of standard listed equity shares, excluding standard listed investment entities and shell companies. We are proposing to implement the new rule and associated guidance in a way that mirrors the existing rule and guidance for premium listed commercial companies.

- 1.14** While we are proposing to bring the rule into effect for issuers of standard listed equity shares (excluding standard listed investment entities and shell companies), we are also seeking feedback on the rationale for (and potential approach to) extending the application of the requirements to issuers of standard listed debt (and debt-like) securities, standard listed issuers of GDRs and standard listed issuers of shares other than equity shares.
- 1.15** Under our proposal, we would require issuers of standard listed equity shares (excluding standard listed investment entities and shell companies) to include a statement in their annual financial report setting out:
- whether they have made disclosures consistent with the TCFD's recommendations and recommended disclosures in their annual financial report
  - where they have not made disclosures consistent with some or all of the TCFD's recommendations and/or recommended disclosures, an explanation of why, and a description of any steps they are taking or plan to take to be able to make consistent disclosures in the future and the timeframe within which they expect to be able to make those disclosures
  - where they have included some, or all, of their disclosures against the TCFD's recommendations and/or recommended disclosures in a document other than their annual financial report, an explanation of why
  - where in their annual financial report (or other relevant document) the various disclosures can be found
- 1.16** As is the case for our current rule for premium listed commercial companies, we propose to issue guidance to help in-scope companies determine whether their disclosures are consistent with the TCFD's recommendations and recommended disclosures. This would include guidance on the level of detail in companies' disclosures. We would also clarify the limited circumstances in which we would expect in-scope companies to explain rather than disclose.
- 1.17** We are also using this CP as an opportunity to generate discussion and engage stakeholders on issues related to ESG-oriented debt instruments and the increasingly prominent role of ESG data and rating providers. These may potentially require further policy intervention to address any potential harms (see Chapter 4).

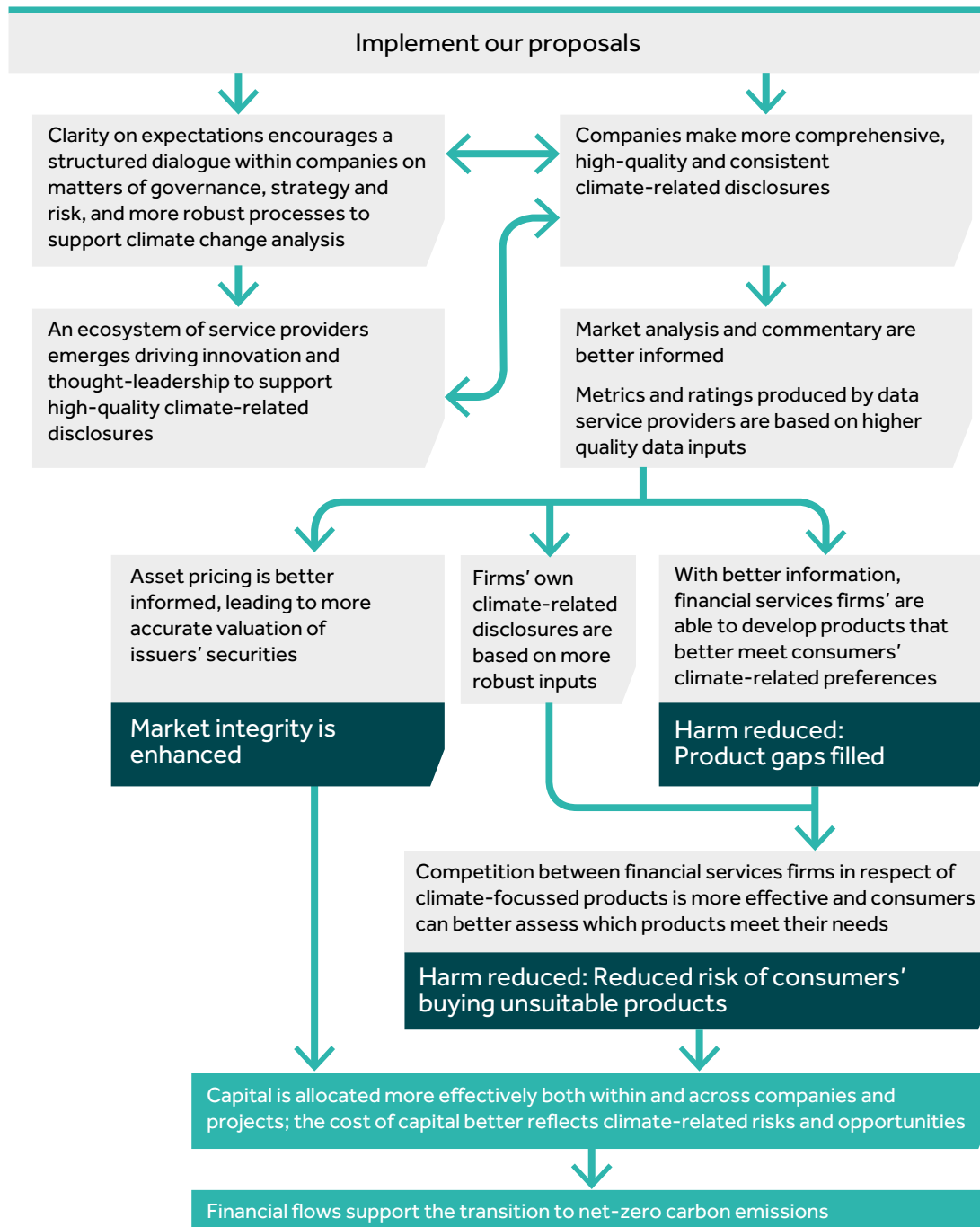
## Outcomes we are seeking

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- 1.18** Voluntary adoption of the TCFD's recommendations continues to increase. However, evidence – from the TCFD's 2020 status report, the Financial Reporting Council's (FRC) climate thematic review, and other reviews of corporate reporting on climate-related matters – suggest that disclosures remain incomplete and that quality remains variable across companies.
- 1.19** So there remains a strong case for regulatory intervention to improve the quantity and quality of climate-related financial disclosures. We discuss the current state of disclosures further in Chapter 2.

**1.20** Figure 1 summarises the causal chain by which we expect our proposals to help address potential harms and deliver benefits for issuers, financial markets and consumers. Since the rationale for intervention is the same as for our existing rule for premium listed commercial companies, the causal chain is as presented in Chapter 1 of CP20/3.

**Figure 1: How enhanced disclosures can help advance our objectives**



**1.21** Consistent with the objectives of our TCFD-aligned disclosure rule for premium listed commercial companies, we are targeting the following main outcomes:

- **Clear regulatory requirements support high-quality disclosures.** Introducing rules that directly reference the TCFD's recommendations will help to make our expectations clear, providing more certainty for issuers, reducing the costs of

meeting ad-hoc information requests, and encouraging in-scope companies to take a structured approach to reporting on climate-related matters. While the TCFD's recommendations do not constitute a corporate reporting standard, implementing TCFD-aligned disclosures will help to build companies' capabilities to identify, assess, manage and disclose on climate-related risks and opportunities. They will then be better prepared when a future corporate reporting standard that builds on the TCFD's recommendations is introduced (see Chapter 2).

- **Better disclosures support more informed business, risk and investment decisions.** More structured disclosures and greater transparency of how investee companies are managing climate-related risks and opportunities will lead to better informed business, risk and investment decisions along the investment chain. This will, in turn, improve asset pricing, reducing the risk that assets are mispriced. Relevant to the FCA's market integrity objective, this translates into fairer and more effective markets.
- **Design of products can more reliably meet consumers' needs.** Improved climate-related financial disclosures by corporate issuers can help support the development of genuinely green financial products. With more complete and higher quality data inputs, firms will have a better understanding of investee companies' underlying climate exposures, enabling them to develop financial products that more reliably meet consumers' needs.
- **Improved allocation of capital.** Improved transparency and asset pricing should in turn support investment and capital allocation decisions. This should also help ensure that issuers can access funding at a cost of capital that appropriately reflects how they manage climate-related risks and opportunities. This will ultimately result in societal benefits arising from better management of climate-related risks and opportunities and capital mobilisation, supporting the transition to a net-zero economy.

## Measuring success

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**1.22** The proposals in this CP are part of a wider set of actions being taken across government, regulators and industry to improve how capital markets manage climate-related risks and opportunities and allocate capital to support the transition to a net zero economy. So, it may be difficult to measure success in a systematic way. That said, we will monitor the success of our intervention in various ways including:

- **Market outcomes.** We will have been successful in our intervention if new disclosures made in line with the proposed rule enable investors and other stakeholders along the investment chain to make more informed investment and capital allocation decisions. This may lead to the market rewarding those companies that are better at adapting and disclosing the risks and opportunities from climate change, particularly as we transition to a net-zero economy. We note, however, that it may not be straightforward to isolate the impact of our measures from other complementary government, regulatory or industry measures to support the climate transition.
- **Oversight.** Our strategic objective is to ensure that relevant markets work well. As part of this, our Market Oversight function has a role to play in ensuring that listed companies make disclosures that support decision-making and enable investors to price securities efficiently and hold such companies to account if their disclosures do not meet the required standard. We committed in PS20/17 to setting out further information on our supervisory strategy in late 2021, ahead of

the first disclosures by companies with a UK premium listing under LR 9.8.6R(8). We will do this in a Primary Market Bulletin later this year. We expect to apply the same supervisory strategy for the proposed new rule for issuers of standard listed equity shares.

- **Supervision of regulated firms.** As part of our regular supervisory dialogue with regulated firms, such as asset managers, we will have opportunities to gather information on the quantity and quality of listed companies' climate-related disclosures and their usefulness in supporting market participants' business, risk and investment decisions.
- **Ongoing industry liaison.** We will continue to gather views on the effectiveness of our regime through industry engagement, including the Climate Financial Risk Forum.

## Next steps

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- 1.23** We invite interested stakeholders to provide feedback on our proposals by 10 September 2021. Please use the online response form on our website or write to us at the address/email address on page 2 of this document.
- 1.24** We will consider the feedback to our consultation proposals with a view to publishing a Policy Statement with the finalised rules by the end of 2021.
- 1.25** We expect to issue a Feedback Statement on responses to our discussion chapter (see Chapter 4) separately. The feedback received will inform our further work in this area.



## 2 The wider context

- 2.1** Better disclosure about companies' exposure to climate-related risks and opportunities will lead to more informed market pricing and help drive investment towards green projects and activities. Improving climate-related disclosures along the investment chain has therefore been central to our sustainable finance strategy.
- 2.2** This chapter provides background on other relevant UK and international initiatives that aim to improve climate-related disclosures. Within this context, we explain the rationale for our proposal to extend the application of our existing TCFD-aligned disclosure requirements for commercial companies with a UK premium listing to a wider scope of listed issuers.

### Background on the Taskforce on Climate-related Financial Disclosures

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- 2.3** The leading framework for making climate-related financial disclosures is the set of recommendations published in 2017 by the FSB's TCFD.
- 2.4** The recommendations span four pillars: governance, strategy, risk management and metrics and targets – with 11 specific recommended disclosures sitting beneath them. These are set out in Appendix 3.
- 2.5** In summary:
- **Governance.** The framework includes specific recommended disclosures on the respective roles of the board and management.
  - **Strategy.** These recommended disclosures cover the nature of the climate-related risks and opportunities that the organisation has identified, the impact they may have, and the resilience to the organisation's strategy under different climate transition scenarios.
  - **Risk management.** TCFD calls for information on the processes the company has in place to identify, assess and manage climate-related risks, as well as transparency on how these are integrated into the organisation's wider risk management framework.
  - **Metrics and targets.** The framework calls for disclosure by companies on the metrics they use to monitor climate-related risks and opportunities, their Scope 1 and 2 emissions, and where appropriate, also their Scope 3 emissions. Moreover, the recommended disclosures cover any climate-related targets the company sets itself and performance against those targets.

### Current status of climate-related disclosures

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- 2.6** In CP20/3 we set out the current status of disclosures at the time, noting relevant studies at the time as part of the rationale for our consultation.

- 2.7** Over the past year, progress has continued to be made in climate-related – and wider sustainability-related – disclosures. The survey, Reporting Matters (World Business Council for Sustainable Development (WBCSD), 2020) revealed considerable improvement in the number of member companies reporting, with 78% of WBCSD member companies in their benchmark having improved their overall score since 2017. The KPMG survey of sustainability reporting similarly found that almost one in five companies in their global survey had reported in line with the TCFD's recommendations, rising to 37% for the largest 250 companies by revenue.
- 2.8** Voluntary adoption of the TCFD's recommendations has continued to increase, with more than 2,000 organisations now publicly supporting the recommendations. According to the TCFD 2020 Status Report, there has been good progress in disclosure against the majority of the TCFD's 11 recommended disclosures (see Figure A2 in the report). However, there is a need for continued improvement. It is clear that disclosures remain incomplete and patchy across the TCFD's four pillars. For each of the recommended disclosures, less than 50% of the companies covered in the analysis were found to be making consistent disclosures.
- 2.9** From a UK perspective, a recent ClientEarth review of the 250 largest listed companies on the UK Main Market found that 40% of companies clearly referred to climate change in their discussion of principal risks and uncertainties in annual financial reports. The report also highlighted a clear difference in the quantity and quality of climate-related disclosures by companies in the FTSE 100 compared with those companies reviewed in the FTSE 250.
- 2.10** The FRC also published a climate thematic review in November 2020. The review examined climate-related considerations by boards, companies, auditors, professional bodies and investors. While the review found that companies were increasingly addressing the risks associated with climate change in their reporting, the FRC concluded that the current level of disclosures did not yet meet the needs of investors and other users.
- 2.11** We therefore consider that, while there have been positive developments in climate-related disclosures, the needs of investors and other market participants are still not being adequately met. Accordingly, there remains a case for regulatory intervention to accelerate progress towards more complete and higher quality disclosures.

## **FCA approach to climate-related disclosures and the link to our objectives**

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- 2.12** The FCA began its work on climate-related disclosures in 2018, as part of a DP on climate change and green finance (DP18/8). In the related Feedback Statement (FS19/6) we set out our priorities for our climate change strategy, including that we would work towards the outcome that 'issuers provide markets with readily available, reliable and consistent information on their exposure to material climate change risks and opportunities'.
- 2.13** We took our first step in this work in March 2020, publishing CP20/3. The CP proposed a new TCFD-aligned disclosure rule for commercial companies with a UK premium listing. We finalised our rule for those listed companies in PS20/17, bringing the rule into force for accounting periods beginning on or after 1 January 2021.

- 2.14** Our existing TCFD-aligned disclosure rule requires in-scope companies to set out whether they have made disclosures consistent with the TCFD's recommendations and recommended disclosures in their annual financial report, on a 'comply or explain' basis. More detail on our existing rule may be found in Chapter 3.
- 2.15** In feedback to CP20/3 we were encouraged by 20 of 55 respondents to extend the application of our rule to a wider scope of listed issuers. With the proposals in this CP, we would expand the coverage of climate-related disclosure rules to all commercial companies that are issuers of listed equity shares, bringing a further 148 companies, with a combined market capitalisation of £974 million, into scope of climate-related disclosure rules.
- 2.16** As set out in CP20/3, if issuers do not make sufficient disclosures, investors' ability to make informed decisions is impaired. This could give rise to harms that impact the financial market, issuers and investors, and potentially also the consumers of financial products. We therefore consider that regulatory intervention to address these harms is compatible with our strategic objective to ensure that relevant markets function well, and would advance our operational objectives to:
- protect and enhance the integrity of the UK financial system
  - secure an appropriate degree of protection for consumers
  - promote effective competition in the interests of consumers
- 2.17** With a lack of clarity about what information investors need to make informed decisions, issuers may not provide decision-useful information to markets on climate-related risks and opportunities. Costs and coordination failures may also lead to issuers failing to make complete and high-quality disclosures voluntarily – we set out further information on this in our cost benefit analysis (see Annex 2). As a result, market integrity may be impaired: assets may be mispriced and investors may be unable to compare asset values, potentially leading to capital misallocation. Issuers may also be unable to access financial markets at the cost of capital they could achieve if investors had more confidence about the impact of climate change on business prospects.
- 2.18** Harms could also arise indirectly. With insufficient information from issuers on climate-related risks and opportunities, financial services firms may find it difficult to design and structure financial products that meet consumers' needs and preferences. Furthermore, financial services firms may be unable to reliably disclose to consumers how their products are exposed to climate change risks and opportunities. This could lead to a higher risk that consumers buy unsuitable products or are subject to greenwashing (ie, they are led to believe that a firm's products have environmental sustainability characteristics when this is not the case).
- 2.19** Accompanying the final rule in PS20/17, we published a Technical Note ([TN 801.1](#)) to clarify existing disclosure obligations in our Handbook and in legislation that may already require disclosures on climate change and other ESG matters under certain circumstances. The Technical Note applies to a wider range of issuers than just commercial companies with a premium listing. We are proposing to update the Technical Note in light of the proposals set out in the CP.
- 2.20** Alongside our work on TCFD-aligned disclosures for listed companies, we have also developed proposals for asset managers, life insurers and FCA-regulated pension providers. These proposals are set out in CP21/17.

- 2.21** The recent remit letter to the FCA from the UK Chancellor also provides an important backdrop to our proposals. The letter provides that the FCA should 'have regard' to the Government's commitment to achieve a net-zero carbon emissions economy by 2050. This is also reflected in the Financial Services Act 2021 and the new s.143G Financial Services and Markets Act 2000 (FSMA) (coming into force from 1 January 2022).

## UK implementation strategy for the TCFD's recommendations

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### Roadmap to mandatory TCFD-aligned disclosures

- 2.22** The UK Government was one of the first to publicly endorse the TCFD recommendations, setting an expectation in its 2019 Green Finance Strategy that all UK listed companies and large asset owners would be reporting in line with the TCFD's recommendation by 2022.
- 2.23** To deliver on this expectation, a cross-Government and regulator taskforce was established to develop an implementation strategy. In November 2020, the taskforce published an Interim Report and Roadmap setting out a path towards mandatory TCFD-aligned disclosure obligations across the UK economy by 2025, with most of the measures anticipated by 2023.
- 2.24** The Roadmap indicated the steps we are proposing for listed companies, asset managers, life insurers and FCA-regulated pension providers.
- 2.25** Also consistent with the Roadmap, DWP has also published draft regulations for trustees of occupational pension schemes.

### BEIS consultation

- 2.26** The Roadmap also set out plans for a legislative provision in the Companies Act 2006 and Limited Liability Partnership (LLPs) Act 2000, to underpin TCFD-aligned disclosures across the economy. BEIS recently conducted a consultation process on proposed TCFD-aligned disclosure provisions.
- 2.27** BEIS has proposed mandatory TCFD-aligned disclosures by certain UK-incorporated companies and LLPs, aligned with the TCFD's recommendations, to come into force for accounting periods beginning on or after 6 April 2022.
- 2.28** The proposed scope includes Public Interest Entities and companies with securities admitted to trading on the Alternative Investment Market (AIM) with over 500 employees, plus LLPs and private companies with over 500 employees and at least £500 million turnover. This creates a partial overlap with the scope of our existing and proposed Listing Rules. We have been working closely with BEIS in order to deliver a coherent disclosure regime for those companies within the scope of both regimes.
- 2.29** The FRC is the relevant enforcement authority for disclosures under the Companies Act 2006. We are therefore also working closely with the FRC to develop a coordinated monitoring and supervision regime.

- 2.30** We committed in PS20/17 to setting out further information on our supervisory strategy for issuers' disclosures under our TCFD-aligned Listing Rule in a Primary Markets Bulletin. This will also describe our work with the FRC.
- 2.31** BEIS is consulting in parallel on wide-ranging proposals to restore trust in audit and corporate governance. While the matters considered in the consultation do not directly impact the climate-related disclosure proposals in this CP, they will have wider implications for the wider corporate reporting landscape in the UK, the audit and assurance industry and the future roles and responsibilities of the FRC.

## International developments

- 2.32** In recent months, strong momentum has built in international initiatives to improve climate-related and wider sustainability reporting. The key initiative is the work of the International Financial Reporting Standards (IFRS) Foundation, which is planning to create an International Sustainability Standards Board (ISSB) to sit alongside the International Accounting Standards Board.
- 2.33** We have been engaged closely with this work as co-chair of a dedicated workstream on issuers' disclosures under the Sustainable Finance Taskforce (STF) of the International Organisation of Securities Commissions (IOSCO). Jointly with the UK Government and other UK financial regulators, we have also publicly voiced our support for the IFRS Foundation's work in this area.
- 2.34** Both IOSCO and the IFRS Foundation recently issued press statements setting out their vision for the new ISSB and the wider corporate reporting regime. The IFRS Foundation is working towards establishing the new ISSB ahead of the UN Climate Change Summit (COP 26) in November, with a view to making quick progress to introduce a climate-related corporate reporting standard. The IFRS Foundation Trustees have signalled that the initial focus will be on climate change.
- 2.35** The IFRS Foundation Trustees are engaged in technical preparations. They have established a Technical Readiness Working Group (TWG), collaborating with TCFD, the World Economic Forum and existing sustainability reporting organisations (including the Sustainability Accounting Standards Board (SASB), the International Integrated Reporting Council (IIRC)<sup>1</sup> and the Climate Disclosure Standards Board (CDSB)) to develop content that can give the new ISSB a running start once it is established.
- 2.36** As part of this, the TWG is exploring how it can best leverage existing content to develop a standard – including the TCFD's recommendations and other existing principles, frameworks and guidance. In December 2020, the five leading voluntary sustainability reporting organisations published a prototype climate-related disclosure standard based on existing content which the TWG is working to refine.
- 2.37** In April, the IFRS Foundation Trustees launched a consultation on potential amendments to its constitution to accommodate the proposed new ISSB, alongside a detailed feedback statement to their original consultation published in late 2020.

1 We note that, on 9 June 2021, SASB and IIRC formally announced the completion of their merger to become the Value Reporting Foundation.

**2.38** We have also seen other jurisdictions implementing or actively working to implement the TCFD's recommendations. For example, in New Zealand, the Ministry for the Environment finalised legislation for listed companies as well as large insurers, banks, non-bank deposit takers and investment managers. Meanwhile in Japan, the Financial Services Agency is currently consulting on changes to introduce TCFD-aligned requirements in its Corporate Governance Code.

**2.39** In the EU, companies subject to the Non-financial Reporting Directive (NFRD) have, since 2019, been encouraged to make climate-related disclosures with reference to a set of non-binding guidelines referencing the TCFD's recommendations. The European Commission is now proposing to enhance climate-related and wider sustainability reporting, integrating and building on the TCFD's recommendations. In April 2021, the European Commission published a proposal for a Corporate Sustainability Reporting Directive (CSRD).

**2.40** The implementation of the TCFD's recommendations and the IFRS Foundation's initiative have also been important areas of focus for the G7, under the UK's presidency. At their meeting in June 2021, G7 finance ministers and central bank governors committed to a 'transformative effort to tackle climate change and biodiversity loss' and emphasised 'the need to green the global financial system so that financial decisions take climate considerations into account'. As part of this, they agreed to support moving towards mandatory climate-related disclosures based on the TCFD framework. They also welcomed the IFRS Foundation's programme of work to develop a baseline global reporting standard for sustainability, built from the TCFD framework and the work of sustainability standard-setters.

### **FCA review of primary markets effectiveness**

**2.41** We support high regulatory standards in the UK, while also ensuring our capital markets are dynamic and effective. Alongside our work to apply the TCFD's recommendations to listed companies, we are also reviewing the effectiveness of UK primary markets in order to ensure the regime continues to meet the needs of both issuers and investors. One aspect of this has been on climate change and wider sustainability matters. The discussion topics set out in Chapter 4 reflect this aspect of our work.

**2.42** Beyond this, in November 2020, the Chancellor announced his intention to review the listings regime, and asked Lord Hill to lead this work. The objective of The UK Listing Review was to propose reforms to the UK listing regime that would attract the most innovative and successful firms and help companies access the finance they need to grow. The findings of this review were published in March and set out a number of areas for us to consider at the FCA, as well as many for HM Treasury to consider.

**2.43** In response to this, we have already published a consultation paper on the role of special purpose acquisition companies (SPACs) in UK markets and will consult on further policy proposals shortly on other areas of our Listing Rules.

### **Equality and diversity considerations**

**2.44** We have considered the equality and diversity issues that may arise from the proposals in this CP.

**2.45** Overall, we do not consider that the proposals materially impact any of the groups with protected characteristics under the Equality Act 2010. But we will continue to consider the equality and diversity implications of the proposals during the consultation period and will revisit them when making the final rules.

**2.46** In the meantime, we welcome any feedback to our consultation on this.

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

- 3.1** In this chapter, we set out in more detail our proposal to extend the application of our existing TCFD-aligned disclosure requirements for commercial companies with a UK premium listing to companies with a UK standard listing of equity shares (excluding standard listed investment entities and shell companies).

### Scope

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- 3.2** The standard listing segment is made up of a number of categories for different types of securities, including shares, debt and debt-like securities, GDRs and securitised derivatives.
- 3.3** We propose to extend the application of our existing TCFD-aligned disclosure requirements (set out in LR 9.8.6R(8)) to issuers of standard listed equity shares (as included in LR 14), excluding standard listed investment entities and shell companies.
- 3.4** In introducing our TCFD-aligned disclosure rules in the Listing Rules, our focus is on the corporate entity itself, rather than on the securities that it issues. This is consistent with the general approach of the TCFD in developing its recommendations, which cover entity-level governance, strategy and risk management arrangements, as well as key entity-level metrics and targets.
- 3.5** Our target coverage is commercial company issuers in the standard listed segment. To achieve this, we propose to apply the rule to issuers of equity shares in LR 14, excluding standard listed investment companies and shell companies. This approach also aligns well with the approach taken in introducing our existing TCFD-aligned disclosure rule for premium listed commercial companies.
- 3.6** However, we also ask a number of questions on whether we should apply our TCFD-aligned disclosure rule to issuers of GDRs in LR 18 (see 3.18-3.20) and standard listed issuers of shares other than equity shares as included in LR 14 (see 3.21). We also ask whether and how we should reflect issuers of standard listed debt and debt-like securities (in LR 17) in the scope of our rule (see 3.22-3.27).
- 3.7** In the case of standard listed investment entities, we consider that a more appropriate approach is to introduce requirements for listed investment vehicles under the framework we are developing for funds managed by UK-authorised firms. As such, some of these will fall within the scope of our proposed TCFD-aligned rules for asset managers (CP21/17).



- 3.8** We also propose to exclude shell companies with standard listed equity shares from the scope of our rule. The form and structure of the TCFD's recommendations would not seem to be appropriate considering such companies' simple balance sheets and that they typically do not have established governance, strategy and risk management arrangements.
- 3.9** With the proposed extension to include issuers of standard listed equity shares, our TCFD-aligned Listing Rules (proposed and existing) would in practice cover all commercial companies who are issuers of listed equity shares. This is consistent with the strong message we received from stakeholders in response to CP20/3 that we should move quickly to extend the scope beyond premium listed commercial companies.
- 3.10** In developing our proposals, we have considered the profile of listed companies that would fall within scope of the proposed rule. Figure 2, below, presents summary statistics on the sectoral and size breakdown of the issuers of standard listed equity shares (excluding standard listed investment entities and shell companies). These show that our proposal would extend the scope of our disclosure requirements to a further 148 companies, with a total market capitalisation of around £1 trillion.
- 3.11** Figure 2(a) shows that in-scope companies span a wide range of sectors, with around half of the companies in the basic resources, financial services and energy sectors. These are sectors in which there is considerable investor interest in companies' climate strategies, including their transition plans. Around half of commercial company issuers of standard listed equity shares are UK-headquartered. The others are headquartered overseas, including countries such as Australia, Ireland, Japan and the US.
- 3.12** Consistent with the principle that all companies within a listing category should be subject to the same rules irrespective of where they are headquartered, we do not propose to differentiate by domicile. The rule would therefore apply equally to all issuers of standard listed equity shares (excluding standard listed investment entities and shell companies).
- 3.13** We do not expect there to be any conflict with overseas headquartered companies' home market rules, since the TCFD's recommendations are an internationally accepted framework. The UK has been one of the 'first movers' to implement TCFD-aligned rules in its legal and regulatory frameworks. However, there is increasing momentum behind similar initiatives in other markets (see Chapter 2). We will keep this under review as other jurisdictions' approaches develop.
- 3.14** Figure 2(b) shows that the size profile of in-scope standard listed companies (as measured by market capitalisation) is weighted towards small and medium sized companies: 92 in-scope companies (around two-thirds of the total number) have a market capitalisation below £250 million. At the other end of the spectrum, 28 companies (19% of in-scope companies) are large, often overseas, issuers with market capitalisations over £2.25 billion.
- 3.15** We noted the size profile of in-scope companies when considering proportionality and the compliance basis of the proposed Listing Rule (see para 3.32), as well as the proposed application of the guidance accompanying the existing rule for commercial companies with a UK premium listing (see para 3.31).

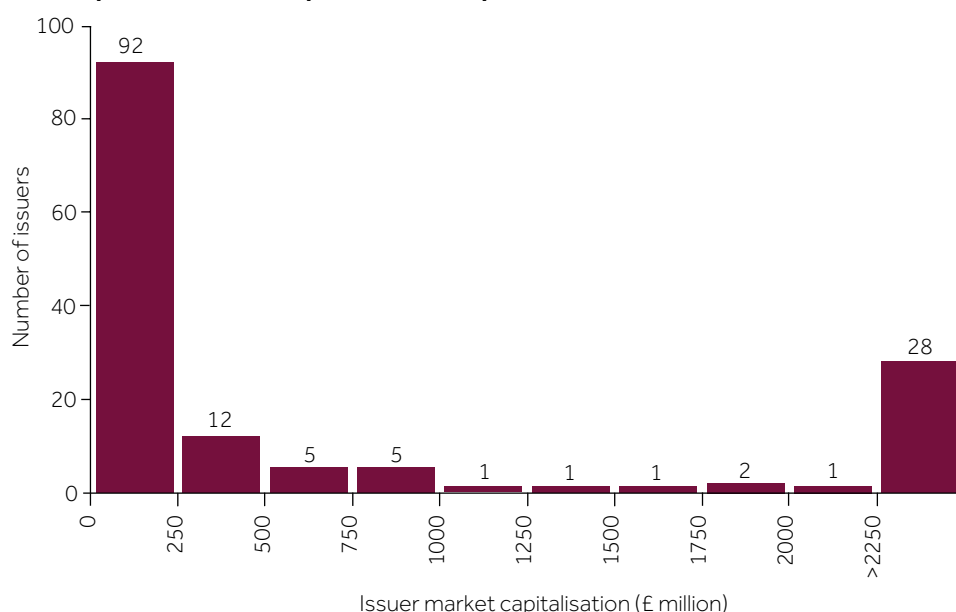
**3.16** The size profile differs markedly from that for premium listed commercial companies, where 18% of the in-scope companies have a market capitalisation less than £250 million, compared to a third of companies having a market capitalisation over £2.25 billion.

**Figure 2: Sectoral and size profile of in-scope issuers**

**(a) Sectoral profile of in-scope listed companies**



**(b) Size profile of in-scope listed companies**



Source: London Stock Exchange statistics, FCA calculations

**3.17** In developing our proposals, we have worked closely with BEIS to ensure that the Listing Rules and Companies Act proposals work effectively together. BEIS has consulted on implementing disclosure obligations closely aligned with the TCFD's recommendations, but with some changes to better embed the requirements into existing Companies Act wording, and with no requirement for scenario analysis. Our Listing Rules, both proposed and existing, build from the same base (the TCFD recommendations), but reference directly the TCFD's 11 recommended disclosures and associated guidance. We have considered the interaction of BEIS's Companies Act proposals with our rules and are confident that in their current form BEIS's proposals and our proposed provisions can work effectively together.

**Q1: 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?**

- 3.18** In implementing our TCFD-aligned disclosure rules for premium listed commercial companies, we also included issuers in LR 21: sovereign controlled commercial companies. The types of securities listed in this premium listing category could either be equity shares or GDRs.
- 3.19** While there are currently no issuers of equity shares or GDRs listed under LR 21, 170 issuers with standard listed GDRs are subject to the continuing obligation requirements in LR 18.
- 3.20** Since GDRs represent the underlying shares in a company, which is typically a commercial company also listed on an overseas market, we welcome views on whether issuers of standard listed GDRs (under LR 18) should also be considered for inclusion within the extended application of our disclosure requirements.
- 3.21** Similarly, we welcome views on whether standard listed issuers of shares other than equity shares should also be included in the extended application of our proposed rule.

**Q2: 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?**

- 3.22** We note that, in its final report, the TCFD encourages that '...all financial and non-financial organizations with public debt or equity implement its recommendations.' Therefore, alongside the application of our proposed rule to issuers of standard listed equity shares (excluding standard listed investment entities and shell companies) – see paragraphs 3.2-3.17 – we have considered applying TCFD-aligned disclosure requirements to commercial company issuers of standard listed debt (and debt-like) securities (noting that many will already be in scope of the existing and proposed rules in their capacity as issuers of premium or standard listed equity shares).
- 3.23** However, the standard listed debt (and debt-like) securities category (LR 17) is very broad and captures a wide range of issuer types. There is currently no separate category for 'commercial company' issuers of standard listed debt and debt-like securities.
- 3.24** Some 10,000 securities are listed under LR 17, issued by approximately 1,000 distinct issuers. Around half of these are overseas-headquartered issuers. These issuers extend well beyond commercial companies to also include, among others, UK and overseas public sector issuers (eg, local authorities and national governments), special purpose funding vehicles (eg, issuers of mortgage-backed securities or other asset-backed instruments) and other non-operating company issuers (eg, healthcare or educational trusts).

- 3.25** With its focus on entity-level organisational factors, such as governance, strategy and risk management, the TCFD's recommendations may not be an effective and proportionate framework for disclosures by certain public sector and non-operating company issuers. For some issuers, prospectus disclosures may be more relevant and decision-useful to investors than annual entity-level disclosures under the four pillars of the TCFD's recommendations – especially where listed debt securities have short maturities.
- 3.26** Accordingly, to help inform whether and how to implement TCFD-aligned disclosure rules for issuers of standard listed debt and debt-like securities, we welcome feedback on what climate-related information from issuers of these securities market participants would find decision useful.
- 3.27** We also welcome views on how best to bring such issuers within scope to deliver an effective and proportionate approach, while avoiding introducing undue complexity and uncertainty to the perimeter for our rule. For instance, we would welcome stakeholder feedback on whether certain issuer types should be excluded from such a rule under LR 17, and if so which types.

**Q3: 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?**
- d. Are there any other matters we should take into consideration – eg, competitiveness, complexity of the application of the rule, burden on issuers in LR 17, or the feasibility to comply with any potential rules?**

## Design of the proposed Listing Rule

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- 3.28** We propose that the new rule – and associated guidance – in LR 14 directly mirror the structure and wording of the rule and associated guidance in LR 9.8.6R(8) and LR 9.8.6BG to LR 98.6EG for premium listed commercial companies. Since the policy

intention for the proposed rule and guidance is the same as that for our existing Listing Rule provisions for premium listed commercial companies, we do not propose to alter the nature of the rule or associated guidance. Furthermore, a consistent approach would avoid fragmentation and support the wider ecosystem that is continuing to develop to support issuers in making their disclosures.

**3.29** Under the proposed rule, we would require in-scope standard listed companies to include a statement in their annual financial report setting out:

- whether they have made disclosures consistent with the TCFD's recommendations and recommended disclosures in their annual financial report
- where they have not made disclosures consistent with some or all of the TCFD's recommendations and/or recommended disclosures, an explanation of why, and a description of any steps they are taking or plan to take to be able to make consistent disclosures in the future, and the timeframe within which they expect to be able to make those disclosures
- where they have included some, or all, of their disclosures against the TCFD's recommendations and/or recommended disclosures in a document other than their annual financial report, an explanation of why
- where in their annual financial report (or other relevant document) the various disclosures can be found.

**3.30** Under the proposed rule, an issuer's statement of compliance may confirm that disclosures consistent with some of the TCFD recommended disclosures have been made, while providing an explanation for non-disclosure in relation to others.

**3.31** We also propose to include the same guidance as is included for the purposes of LR 9.8.6R(8) in LR 9.8.6BG to LR 9.8.6EG. These guidance provisions include:

- a. Guidance that in-scope listed companies should consider whether their disclosures provide sufficient detail to enable users to assess the company's exposure to and approach to addressing climate-related issues. Moreover, that in-scope listed companies should assess the appropriate level of detail to be included in their climate-related financial disclosures. The assessment should take into account factors such as the level of their exposure to climate-related risks and opportunities, and the scope and objectives of their climate-related strategy. The guidance notes that these factors may relate to the nature, size and complexity of the listed company's business.
- b. Guidance clarifying that we expect an in-scope listed company's determination of whether its climate-related financial disclosures are consistent with the TCFD's recommendations and recommended disclosures to be informed by a detailed assessment of those disclosures which takes into account specified TCFD guidance materials in the TCFD Annex (Section C of the TCFD Annex, entitled 'Guidance for All Sectors'; (where appropriate) Section D of the TCFD Annex, entitled 'Supplemental Guidance for the Financial Sector'; and (where appropriate) Section E of the TCFD Annex, entitled 'Supplemental Guidance for Non-Financial Groups').
- c. Guidance clarifying other TCFD guidance materials that we consider relevant to the in-scope listed company's determination of whether its disclosures are consistent with the TCFD's recommendations and recommended disclosures.
- d. Guidance clarifying the limited circumstances in which we would expect a listed company to explain, rather than make disclosures, noting that we would ordinarily expect an in-scope listed company to be able to make climate-related financial disclosures consistent with the TCFD recommendations and recommended

disclosures, except where it faces transitional challenges in obtaining relevant data or embedding relevant modelling or analytical capabilities.

- 3.32** We consider the guidance in (a) to be particularly impactful for smaller companies within scope of the proposed rule. The guidance explicitly notes that the appropriate level of detail for an in-scope listed company's disclosures may be linked to the nature, size and complexity of its business.
- 3.33** We note also that, by mirroring the structure and wording of LR 9.8.6R(8), we are proposing to have the same 'comply or explain' compliance basis. As set out in paragraph 3.31 we are proposing to mirror the guidance provision which clarifies the circumstances in which we would expect issuers to explain rather than make disclosures. As in LR 9.8.6R(8), we are also proposing that where issuers have not made disclosures consistent with some or all of the TCFD's recommendations and recommended disclosures, they should set out any steps they are taking – or plan to take – to be able to make such disclosures consistently in the future.
- 3.34** We consider this an appropriate and proportionate approach, noting that the rationale for initially adopting a 'comply or explain' approach for premium listed companies, as set out in CP20/3, continues to hold for the proposed wider scope of listed companies, especially for smaller (by market capitalisation) listed companies where capabilities are still developing. In particular, the evidence suggests that issuers still face challenges in preparing climate-related financial disclosures, in part due to outstanding definitional issues unrelated to our rules (proposed and existing), challenges in creating the primary data and the need to develop internal capabilities.
- 3.35** So we still see the need for an approach that fosters best practice but that will not force issuers into making disclosures they cannot confidently support, or that may discourage them from making best efforts. A more flexible approach, using a 'comply or explain' basis, would allow issuers to develop their approaches and adapt as this area continues to evolve. See also paragraphs 3.48 to 3.56.
- 3.36** In 2020, the TCFD published a consultation on Forward-Looking Financial Sector Metrics. In June 2021, TCFD issued a further consultation on metrics, targets and transition planning. This consultation proposes:
- a.** updates to the TCFD's existing all-sector guidance (contained in the TCFD Final Report and TCFD Annex), and to the supplementary guidance for both non-financial and financial sectors (contained in the TCFD Annex)
  - b.** additional guidance in a standalone document on metrics targets, and transition planning
- 3.37** On the assumption that the TCFD's updates to the guidance in (a) remain broadly consistent with that proposed in the consultation, we consider that it would be appropriate to incorporate these into our Handbook guidance provisions when we finalise our policy position – both in our existing guidance supporting LR 9.8.6R(8), and our proposed guidance in this CP supporting LR 14.3.27R. We propose to do this by amending the definition of the 'TCFD Final Report' and 'TCFD Annex' set out in our Handbook Glossary. This will feed into the existing guidance in LR 9.8.6BG and LR 9.8.6CG and our proposed guidance in LR 14.3.28G and LR 14.3.29G.
- 3.38** Similarly, subject to the TCFD's final guidance in the proposed standalone document on metrics, targets and transition planning being broadly consistent with the content

in the consultation, we consider that it would also be appropriate to reference the proposed standalone guidance document in our existing and proposed Handbook guidance in LR 9.8.6GC and LR 14.3.28G.

**3.39** Also in June 2021, the TCFD issued for consultation a technical supplement on measuring portfolio alignment. Again, subject to the final version of the technical supplement being broadly consistent with the consultation version, we propose to reference the final technical supplement on measuring portfolio alignment in our guidance (specifically LR 9.8.6CG and LR 14.3.28G).

**3.40** We have set out the drafting of the proposed Handbook guidance, as well as amendments to existing guidance provisions, and the proposed change to the Handbook Glossary (including a definition for the technical supplement), in the draft instrument in Appendix 1.

**3.41** Finally, as a result of the proposed rule in this CP, we consider it appropriate to update Technical Note 801.1. In particular, we propose to reflect the proposed new rule and associated guidance, LR 14.3.27R and LR 14.3.28G – LR 14.3.31G, in the section on the Listing Rules. We are not proposing any further changes to the Technical Note. A draft of the updated Technical Note is included in Appendix 2.

**Q4:** 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?

**Q5:** 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
- b. the TCFD's proposed standalone guidance document on metrics, targets and transition planning
- c. the TCFD's technical supplement on measuring portfolio alignment.

If not, what alternative approach would you prefer?

**Q6:** Do you agree that we should update the Technical Note 801.1 to reflect the proposed new rule and associated guidance in this CP?



## SASB metrics

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- 3.42** The TCFD's recommendations provide for a robust framework under which to make climate-related financial disclosures. However, we acknowledge that they fall short of a corporate reporting standard and that additional specificity and granularity may be necessary in some areas in order to provide the consistency and comparability of disclosures that investors need.
- 3.43** The TCFD's forthcoming updated guidance on metrics, targets and transition planning referenced above (paragraph 3.36) will add helpful specificity. And, in due course, consistency and comparability of disclosures is expected to be supported by the baseline international reporting standard on sustainability that the IFRS Foundation is working towards (see Chapter 2).
- 3.44** In the meantime, existing voluntary frameworks may helpfully complement the TCFD's recommendations. These include the SASB Standards, which have been developed to guide corporate disclosure of financially materially sustainability information by companies, with an investor focus.
- 3.45** They comprise 77 Industry Standards, identifying industry-specific disclosure topics and metrics (the SASB metrics). The SASB Standards are maintained under the auspices of the new Value Reporting Foundation, established as a result of a merger between SASB and the IIRC, which was concluded on 9 June 2021.
- 3.46** The SASB metrics provide helpful specificity to complement the TCFD's recommendations (noting that the SASB metrics extend beyond climate change related matters). The FRC acknowledged this in its climate thematic review in 2020, encouraging 'UK public interest entities to report against the TCFD 11 recommended disclosures and, with reference to their sector, using the SASB metrics'.
- 3.47** We do not propose to reference SASB metrics directly in our Listing Rules. However, consistent with the FRC's encouragement to UK public interest entities, we encourage relevant listed companies to consider the SASB metrics for their sector when making their disclosures against the TCFD's recommended disclosures.

**Q7: 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.**

## Review of the 'comply or explain' compliance basis

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- 3.48** We introduced our TCFD-aligned disclosure rule for premium listed companies with a 'comply or explain' compliance basis. In both the Roadmap and PS20/17, we said we would review the compliance basis for our existing rule and for our proposed rule for standard listed companies.
- 3.49** We received strong feedback from some stakeholders – mostly asset managers and civil society organisations – to CP20/3 that we should move quickly to mandatory disclosure requirements.



- 3.50** While we strongly support a pathway to mandatory climate-related disclosures, we do not believe that now is the right time to consult on transitioning our TCFD-aligned Listing Rules to a mandatory compliance basis.
- 3.51** This in part reflects that capabilities continue to build among relevant listed companies, particularly smaller listed companies (see paragraph 3.14). Therefore, it is important to retain some flexibility in the compliance basis.
- 3.52** Furthermore, since the publication of the Roadmap in November 2020, the momentum behind the IFRS Foundation initiative to establish an ISSB has accelerated faster than we had expected. As set out in Chapter 2, there is a realistic prospect that the IFRS Foundation will have established an ISSB by the time of COP 26 in November 2021. The IFRS Foundation Trustees have committed to build from the TCFD's recommendations and the content of the existing sustainability reporting organisations. An Exposure Draft for a common international reporting standard for sustainability, starting with climate change, could be issued in the first half of 2022.
- 3.53** An international reporting standard that adds specificity to the TCFD's recommendations – in particular in relation to the metrics and targets pillar – is likely better to support a mandatory compliance basis for issuers, as well as an audit and assurance framework for such disclosures. It would also support the consistency, comparability and reliability that asset managers require. The appropriate time to consult on moving to a mandatory compliance basis is therefore likely to be once the new reporting standard has been introduced in the UK.
- 3.54** We appreciate that any such standard will need to go through a UK adoption process, which could take some time. We would also need to consult on amending our rules to reference the new standard, rather than the TCFD's recommendations.
- 3.55** However, we think that it is important to take stock of how the IFRS Foundation's initiative develops in the coming months before proposing to move our rule (both for premium listed issuers and for standard listed issuers as proposed in this CP) to a mandatory compliance basis. We have started discussions with BEIS on how a UK framework for the adoption of the ISSB standard could work.
- 3.56** If the implementation of a common international standard is materially delayed, we would expect to consult on moving our existing TCFD-aligned disclosure rule to a mandatory compliance basis, in line with the timeline in the Roadmap.

**Q8:** 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?

## The role of audit and assurance

- 3.57** In implementing our TCFD-aligned disclosure rule for premium listed commercial companies, we did not require third-party audit or assurance on the underlying disclosures or the statement of compliance. However, we indicated the important role for assurance in the long term.

- 3.58** As set out in our response to the feedback on the relevant question in our Policy Statement (PS 20/17), we have continued considering the case to introduce a requirement for third-party assurance relating to the underlying disclosures or the compliance statement.
- 3.59** While there have been developments by the audit and assurance industry, including recent guidance by the International Audit and Assurance Standards Board (IAASB) to help advance assurance for non-financial reporting, we consider that the industry is still developing its approach to climate-related disclosures. We also note the ongoing work in the UK in relation to audit reforms, on which BEIS issued a [consultation paper](#) in March.
- 3.60** We therefore propose not to change our position for both the existing and proposed Listing Rules in relation to audit and assurance of the underlying disclosures or the statement of compliance. However, we reiterate that we see significant value in third-party audit and assurance of listed companies' climate-related disclosures in the longer term, and encourage issuers to continue to consider obtaining third-party verification or assurance on a voluntary basis.
- 3.61** We will continue to monitor developments in relation to audit and assurance of climate-related disclosures and continue to keep our position under review, noting that a formal corporate reporting standard such as that being developed by the IFRS Foundation (see Chapter 2), once in place, would likely form a sound basis for an appropriate audit and assurance framework.

**Q9: 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?**

## Timing

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- 3.62** We propose that the new rule take effect for accounting periods beginning on or after 1 January 2022. This would mean that the first annual financial reports issued in compliance with the proposed rule would be published in 2023.
- 3.63** We consider this implementation timeframe to be appropriate, acknowledging that we have clearly signalled the proposed extension, both through our commitments in the Roadmap, and in finalising our policy for premium listed commercial companies (PS20/17).
- 3.64** We recognise that many proposed in-scope standard listed companies are smaller than premium listed companies in-scope of LR 9.8.6R(8), and therefore may face transitional challenges. However, any delay to implementing the proposed rule would not be in the public interest and would fail to acknowledge growing demand among market participants for this information. We also note the proposed 'comply or explain' basis for compliance.

- Q10:** Do you agree that our new rule should take effect for accounting periods beginning on or after 1 January 2022? If you consider that we should set a different timeframe, please explain why.
- Q11:** Do you agree with the conclusions and analysis set out in our cost benefit analysis (Annex 2)?

## 4 Discussion topics on ESG integration in UK capital markets

### Background

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- 4.1** We have been considering the integration of wider ESG matters in UK capital markets as part of a review of the effectiveness of primary markets (see Chapter 2). Through this work, we are promoting the wider public interest with a view to being world-leading, including on ESG.
- 4.2** To inform our ongoing policy work, we are looking to generate discussion and engage stakeholders on the following topics:
- a.** Issues related to green, social or sustainability labelled debt instruments
    - i.** Prospectus and 'use of proceeds' bond frameworks
    - ii.** The role of verifiers and second party opinion (SPO) providers
  - b.** ESG data and rating providers
- 4.3** We recognise that in developing any future policy position on these issues, we will in many cases need to work with others, including the Treasury. We are already engaging closely with the Treasury in relation to Government's wider net-zero strategy and sustainable finance-related disclosure strategies. The feedback from this discussion chapter will inform our ongoing dialogue.

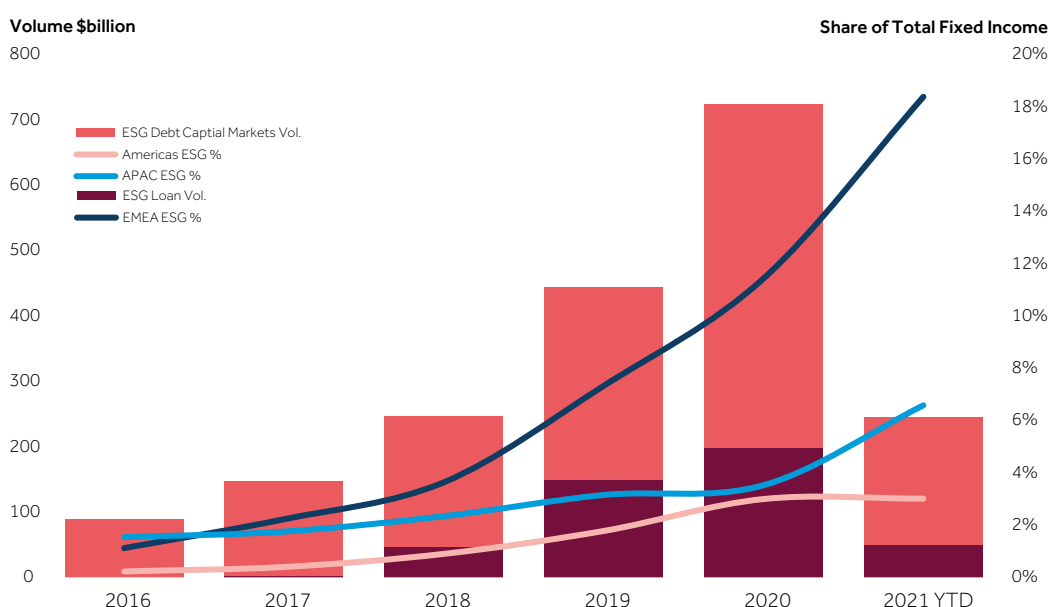
### Issues related to green, social or sustainability labelled debt instruments

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- 4.4** The market has seen a proliferation of product development with rapid growth in Use of Proceeds (UoP) bonds and also more recently sustainability-linked bonds (SLBs) across the ESG spectrum.
- a.** UoP bonds are a standard recourse-to-the-issuer debt obligation for which the proceeds are used for a specific project or to finance a sustainable economic activity that is linked to the issuer's investment framework for eligible projects. The market has developed various types of these instruments including green bonds, social bonds, blue bonds and sustainable bonds.
  - b.** An SLB is any type of bond instrument for which the financial and/or structural characteristics (typically the coupon) can vary depending on whether the issuer achieves predefined sustainability and/or ESG objectives. These objectives generally refer to sustainability performance targets (SPTs), supported by more detailed key performance indicators (KPIs).

- 4.5** A number of potential issues may arise in the market for green, social, sustainable debt instruments. Many of these relate to the market-led development of these instruments.
- 4.6** UoP bonds make up the majority of issuance to date. This, in part, reflects the development of various principles to help support issuance in this market. The first green UoP bond was issued by the European Investment Bank (EIB) in 2007. In recent years, there has been a significant increase in the amount of ESG labelled debt (see Figure 3). 2020 was another record year for issuance, with a significant increase in social labelled debt in response to the coronavirus pandemic.
- 4.7** More broadly, global ESG bonds and syndicated loans reached a combined volume of \$239.1 billion in early 2021. This represents an 8.8% share of the total fixed income market.

**Figure 3: ESG bond and loan issuance volume by region and security type**

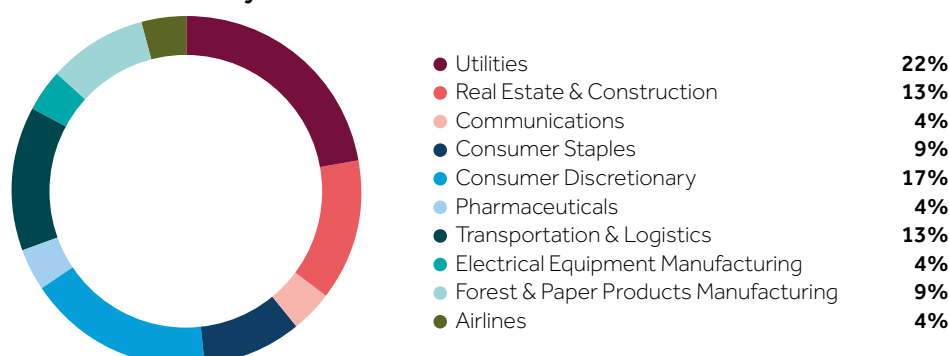


Source: Dealogic Insights

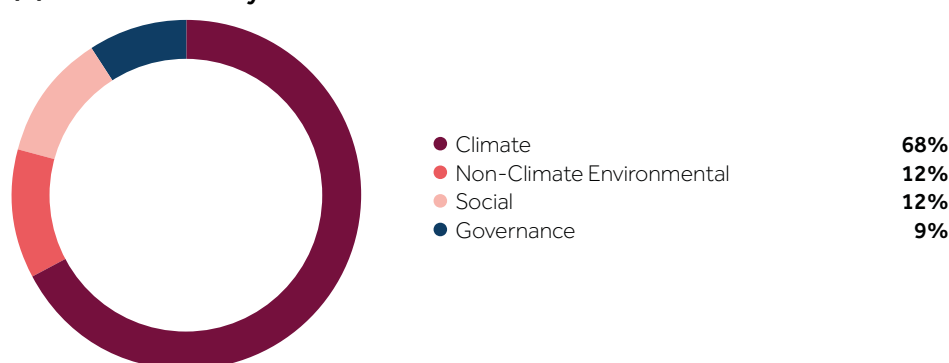
- 4.8** SLBs, on the other hand, are a more recent development. While there has been a lower volume of issuance of SLBs globally, these have been issued in a range of different sectors (see Figure 4(a)). Unlike UoP bonds which are used to fund specific projects, SLBs can be used to finance an entity's sustainability transition and overall progress. They typically embed triggers for financial adjustments, most often on the coupon, referencing certain sustainability-related targets. At present, the KPIs referenced in SLBs' targets are predominately related to climate change matters, as set out in Figure 4(b).

**Figure 4: SLB issuance by sector and KPIs by theme**

**(a) SLB issuance by sector**



**(b) Share of KPIs by theme**



Source: ICMA quarterly newsletter via Nordea, Bloomberg

## Prospectuses and 'Use of proceeds' Bond Frameworks

- 4.9** We have examined a number of prospectuses and supplementary prospectuses for UK-issued green UoP bonds. The language used in the documents confirms our understanding that, in general, while they are marketed as UoP bonds, the contractual terms contained within the prospectus may not fully reflect the information in the bond framework.
- 4.10** That is, the contractual terms may not fully reflect information on the types of projects or activities for which the issuer will use the proceeds; the management of proceeds; the related reporting by the issuer; and details of any third party provider the issuer engages to provide a second party opinion (see below).
- 4.11** In general, we have found that the language used typically seeks to impose limitations on the use of proceeds only on a best endeavours basis, rather than on a fully contractual basis. Accordingly, failure to meet the use of proceeds terms does not constitute an event of default. The language also often limits the reliance and legal liability on verifiers and SPO providers.

**4.12** There are perhaps valid reasons why the market has developed in this way. For instance:

- **Definition of sustainable activities.** Issuers and their advisors need to manage potential liabilities arising from the absence of regulatory and market standards regarding what activities and projects should be considered 'sustainable'. Ongoing work by Government to develop a Taxonomy for sustainable activities should, in time, resolve some of these issues.
- **Rapid market growth.** There is arguably considerable pressure on investors currently to accept less stringent contractual protections. In part, this reflects broader market trends, with green, social or sustainability labelled debt issuances often being heavily oversubscribed. For example, in H2 2020, EUR green bonds were on average 4.2x oversubscribed compared to vanilla bonds which were only 2.9x oversubscribed.

**4.13** While only a small proportion of all issuance, there have been cases where the issuer has failed to deploy the proceeds in the types of projects that it originally set out to fund. This has sometimes led to significant market disruption and significant price fluctuations. One such example is the green bond issued by Mexico City Airport Trust to fund a new airport. The airport project was later abandoned. We consider that these failures may also increase the reputational risk for the wider market.

**4.14** There has also been some debate on this topic in the EU. For instance, the French Autorité des Marchés Financiers (AMF) and Dutch Autoriteit Financiële Markten (AFM) have encouraged further consideration of the disconnect between an issuer's green bond framework and the contractual terms of issuance.

**4.15** While the AMF/AFM paper stopped short of suggesting a 'full' prospectus for green bonds, the two regulators instead considered that 'investors should at least get access to sufficient and reliable information on the 'use of proceeds' by an issuer raising capital through green bonds'. They conclude that an adequate solution could be to bring targeted amendments to Level 2 of the Prospectus Regulation to require additional minimum information in the 'use of proceeds' section of a prospectus where the bond issuance makes 'green' claims.

**Q12:** 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?

**Q13:** Should the FCA explore supporting the UoP bond market by recognising existing standards (eg, ICMA Principles), potentially through our recognition of industry codes criteria and process?

**Q14:** 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.

## The role of verifiers and second party opinion providers

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- 4.16** We understand that the second party opinion is considered a key part of an issuer's pitch to investors on the debt instruments they plan to issue. SPOs have typically been designed with a view to providing investors with assurance (not in an audit capacity) that the use of proceeds for related bond issuances are aligned to market practices or principles. SPO providers often also comment on the link between the use of proceeds and the issuer's wider sustainability strategy. The SPO is normally based on a framework published by the issuer setting out how it will use the proceeds to finance projects from the bonds it plans to issue.
- 4.17** The use of SPOs has become a key requirement of the market as it has developed. The majority of issuers now engage an external review – in 2019, over 90% of issuances by value, globally, used an SPO provider. However, at present, both SPO providers and verifiers are outside of our regulatory perimeter.
- 4.18** While there are a number of providers in the market, it is becoming increasingly concentrated. In the last 18 months we have seen some significant transactions in this sector, many of these also involving the consolidation of other ESG data and ratings businesses (see paragraph 4.36).
- 4.19** The role of verifiers and SPO providers needs to be carefully considered for the different current bond structures – UoP and SLB – as there are some important differences for each bond structure.
- 4.20** The role of SPOs is typically time-limited when it comes to supporting an issuer of UoP bonds, as their engagement will be focussed at the start of the process, when the relevant bond framework is being drafted, until it is published.
- 4.21** As noted above, few of the UoP bonds that we reviewed contained tight contractual clauses on the use of proceeds or, for that matter, any other aspect of the bond framework, including whether the issuer had sought a second party opinion at issuance or verification post-issuance.
- 4.22** Conversely, for SLBs, the sustainability KPIs are carefully described in the prospectus, as are the related SPTs. This reflects that a defining feature of an SLB is that the bond's structural characteristics can vary depending on the issuer's performance against the predefined SPT(s). This means that the SLB's prospectus will need to describe the financial and/or structural impact arising from a trigger event(s).
- 4.23** This leads to a critical role for verifiers. Issuers typically seek independent, third party verification, on a limited or reasonable assurance basis, of their performance against their SPT(s). This external verification will need to happen at least once a year – or during a relevant performance assessment period, specified in the SLB's prospectus.
- 4.24** We see a number of potential sources of harm in the SPO/verifier market that could impact trust in the opinions, due diligence and verification they provide – with implications for the broader market for ESG labelled debt instruments.
- 4.25** These include the harm that may crystallise because of the conflict of interest between the SPO provider/verifier and the investors reliant on it in an 'issuer pays model'. This is potentially exacerbated by the lack of transparency on the methodology used to support the SPO. This relationship may be further complicated where the SPO



provider/verifier is also providing ESG ratings and other related services to the issuer (see section on ESG data and rating providers below).

**4.26** There may also be a more specific harm in relation to SLBs given the potential complexity in analysing and assuring performance against SPTs. There is a potential challenge in building the skills and gaining the necessary access to the issuer to effectively assess KPIs. The quality of the issuer's disclosures may also play a role in the verifier's ability to analyse against the SPTs.

**4.27** The EU Commission has taken the approach that for securities issuance aligned with the proposed EU Green Bond Standard, relevant SPO providers and verifiers will come under the oversight of European Securities and Market Authority (ESMA).

**Q15:** We would welcome views on the potential harm set out above and what, if any, actions the FCA or the Treasury should consider.

**Q16:** Should the FCA, alongside the Treasury, consider the development and creation of a UK bond standard, starting with green bonds?

## ESG data and rating providers

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**4.28** This section considers some of the issues that arise from the increasingly prominent role that ESG data providers – and, in particular, ESG rating providers – are playing in financial markets.

**4.29** This is an active area of debate, with several other regulators having considered this issue recently – mostly in Europe. In December 2020, the French AMF and Dutch AFM issued a [position paper](#) proposing a European regulatory framework for ESG data, ratings and related services. Their particular focus was on transparency and conflicts of interest.

**4.30** In January 2021, ESMA similarly [wrote](#) to the European Commission, setting out its concerns that these prominent services are currently unregulated and unsupervised, and calling for legislation to introduce a robust regulatory framework.

**4.31** We are also currently participating in a workstream on ESG data and rating providers under IOSCO's Sustainable Finance Taskforce. This work is considering some of the issues raised in this section.

### The ESG data and rating landscape

**4.32** There is no firm definition of ESG data provision, which comprises a wide range of data and analytics services. For instance, services include: platforms for access to raw data (in some cases looking through directly to companies' annual reports or other sustainability disclosures); analytical tools to capture, manipulate and analyse data; and packaged data, such as periodic reports based on surveys and questionnaires.

**4.33** Opimas [estimates](#) that the market for ESG data was around \$600 million in 2019. With an expected annual growth rate of 20% for ESG data, and 35% for ESG indices,

the market could approach \$1 billion in 2021. According to the Opimas analysis, asset managers are the largest users of this information, including raw data and ESG ratings.

- 4.34** While some common issues arise across the different types of ESG data and rating providers – for instance, users' reliance on, and the governance and transparency of services/methodologies – our particular focus here is ESG ratings. ESG ratings are ordinal rankings of companies' ESG performance and are distinct from the consideration of ESG factors within credit rating agencies' (CRAs') assessments of companies' creditworthiness.
- 4.35** While a large number of ESG data and rating providers offer services internationally, the vast majority of these are small, niche providers specialising in specific sectors, or covering specific ESG attributes. By 2018, more than 600 ESG ratings and rankings existed globally, according to SustainAbility.
- 4.36** There has been significant consolidation among the leading ESG rating providers over the past decade. For instance, MSCI acquired Innovest and KLD in 2009 to establish its ESG research business; Moody's acquired Vigeo Eiris in 2019; Morningstar acquired Sustainalytics in early 2020; S&P Global completed its acquisition of RobecoSAM in January 2020; and the London Stock Exchange Group – which owns FTSE Russell – completed its acquisition of Refinitiv in 2021.
- 4.37** As demand for ESG-integrated and sustainability-themed investments grows, firms want to be able to meet their clients' needs as efficiently as possible. Some firms may consider it efficient to supplement their own company-level ESG data analysis with inputs from one or more third-party ESG data and rating providers.
- 4.38** Firms are also increasingly building references to third-party ESG ratings into the design and delivery of their sustainable investment products.
- 4.39** Some asset managers and investors now embed ESG rating targets or thresholds in their investment processes. For instance, they may incorporate ESG ratings into their stock selection processes or other elements of their investment strategies.
- 4.40** Others include ratings in their consumer disclosures to describe the ESG characteristics of investments. Benchmark providers also use third-party ESG ratings in the design of indices and benchmarks. A recent [survey](#) by SustainAbility, found that 65% of institutional investors use ESG ratings at least once a week in their work.

### **Challenges arising from the role of ESG data and rating providers**

- 4.41** While not specific to ESG data and rating services, under our existing Handbook rules, asset managers who rely on third-party services are expected to have carried out a level of due diligence on their providers.
- 4.42** For instance, as part of its duty to act in the best interests of the scheme and its unitholders, an authorised fund manager of a UCITS scheme would (under COLL 6.6A) be expected to 'exercise due skill, care and diligence when entering into, managing or terminating any arrangement with third parties in relation to the performance of risk management activities' and 'establish methods for the ongoing assessment of the standard of performance of the third party'.

- 4.43** It might reasonably be expected that such due diligence obligations would extend to considering the fitness for purpose of these services in meeting the asset manager's information needs, and their duty to act in the best interests of their clients.
- 4.44** In the case of ESG ratings, however, interpretation is inherently challenging. Two issues in particular arise:
- **ESG performance is by its nature multi-dimensional.** Accordingly, each ESG rating provider makes different choices about which ESG factors to consider in its methodology, and which metrics to use to measure performance on each of these attributes. Each provider also combines these metrics in a different way, applying different weighting and aggregation methodologies. This is significantly different to credit ratings where creditworthiness is fairly easily defined as the 'likelihood of receiving full and timely payment of interest and principal'.
  - **ESG ratings are subject to data gaps.** ESG ratings are typically subscription services, and hence generally provided on an 'investor pays' basis. As a result, there is typically no contractual relationship between the rated company and the rating provider governing the provision of data to support the provider's rating judgement. Accordingly, rating providers generally rely on public data combined with companies' voluntary submission of responses to periodic questionnaires or surveys. This contrasts with the 'issuer pays' model in the case of credit ratings, under which the contractual basis includes a non-disclosure agreement to support the sharing of confidential information. While an 'investor pays' model mitigates some of the concerns that might arise from conflicts of interest (see Table 1), the 'arms-length' nature of the interaction with issuers potentially leads to data gaps or misinterpretation of corporate information. Rating providers may then take different approaches to filling remaining data gaps.
- 4.45** It is therefore perhaps not surprising that the correlation between different providers' ESG ratings is relatively low. One recent study (Berg, Koelbel and Rigobon (2020)) calculated an average overall correlation of 0.54 across the six rating providers in their sample – much lower than the 0.98 correlation observed between the largest three credit rating agencies. The authors concluded that the main reason for such divergence was the ESG rating agencies' different methodologies to measure ESG performance, followed by differences in the scope of ESG matters considered. The different weighting attached to different ESG factors in providers' methodologies was found to be less important.
- 4.46** A paper by Kotsantonis and Serafeim (2019) considers data gaps. The authors describe the alternative approaches a rating provider may take to fill data gaps. These include: applying a rules-based approach (eg, applying either the average or worst-case performance for the relevant region or sector); scaling relevant industry metrics; or using regression and other statistical imputation methods.
- 4.47** Improved availability of ESG information to fill these gaps will not necessarily increase convergence of ratings. A recent paper by Christensen, Serafeim and Sikochi (2021) found that greater ESG disclosure by corporates actually leads to *increased* disagreement across ESG rating agencies. This implies that better data inputs exacerbate the divergences arising from providers' different approaches to scope and measurement.
- 4.48** Of course, divergence is not inherently undesirable, as long as there is appropriate transparency on the methodologies and that these are robust. If ratings are merely

used as research inputs, divergence of different providers' ratings could improve market functioning. After all, efficient market pricing relies on trading between actors with different views.

**4.49** However, combined with other features of ESG rating provision, there may be potential for harm to market functioning, or to consumers, in some circumstances. Given the different nature of ESG rating services relative to other ESG data services, the potential for harm is likely to be higher for ESG rating provision:

- **Hardwiring of ratings into investment processes.** As ESG-oriented investment strategies become more prominent across markets, ESG ratings may increasingly be embedded into firms' investment processes. Ratings may therefore have a greater impact on investment outcomes for consumers, especially where they are used to create the indices applied in ESG-tilted index strategies.
- **Lack of transparency of methodologies and interpretability of ratings.** With relatively limited transparency of providers' methodologies, firms' clients and consumers may be unable to easily interpret what the ratings represent and how they may affect investment outcomes. This is exacerbated by the absence of common definitions and terminology. Furthermore, given the variability in ratings among providers, the particular choice of rating referenced in investment processes, contracts, benchmarks or indices could also have implications for the allocation of capital. The lack of transparency of providers' methodologies may also lead to misunderstandings or misperceptions as to how they address certain ESG factors in their ratings. As an example, Boohoo was rated highly by several ESG rating providers when adverse news stories surfaced around the treatment of workers in its supply chain. This raised questions as to whether and how such matters should have been reflected in the providers' methodologies, and how the providers might have been expected to adjust their ratings in response.
- **Governance and conflicts of interest.** Given the growing importance of ESG ratings in investment processes, good governance of providers' ratings processes is essential. Users of ratings will want to be confident, among other things, that the process is subject to sound systems and controls and that methodologies are subject to ongoing review and validation. Furthermore, some ESG rating providers provide services to issuers other than ratings, either in other business lines, or through the provision of consulting services on how issuers can enhance their ratings. This could potentially lead to conflicts of interest, even in an 'investor pays' model. There is also a clear interaction here with the concerns raised about conflicts in the section above on SPO providers and verifiers.
- **Engagement with issuers and the cost of meeting providers' data requests.** ESG rating providers supplement public data by requesting issuers respond to questionnaires. These are often lengthy, and we understand that there is rarely much consistency among the questionnaires. It is therefore costly to respond to requests from multiple rating providers. Issuers may therefore prioritise responses to certain ESG rating providers. The criteria they apply in such prioritisation could potentially lead to some market distortion. Some issuers have observed that there is also often limited opportunity to correct misunderstandings or misinterpretation of their responses by the rating provider.

## Policy responses

**4.50** In considering the case for regulatory intervention to address the potential harms set out above, it is instructive to compare the current policy concerns about ESG rating providers with those that prompted regulation of CRAs (or increased regulation) in

many jurisdictions after the 2008-09 financial crisis. Table 1, below, shows that there are some similarities, but also important differences.

- 4.51** For instance, concerns about ratings methodologies and transparency are common to both CRAs and ESG rating providers, as are concerns about how ratings are embedded into financial contracts and investment processes. However, the degree of such hardwiring of ESG ratings appears currently to be more limited than was the case for CRAs at the time of the crisis.
- 4.52** The scope for conflicts of interest may also be lower for ESG rating providers. Conflicts have been a significant policy concern in the case of CRAs, given that their principal revenues typically derive from fees from rated issuers. In the typical 'investor pays' model, ESG ratings provider revenues derive principally from subscriptions by investors and other users. However, as noted, conflicts could arise where firms provide consultancy or other services to rated companies elsewhere in their business, or if there were a shift towards an 'issuer pays' market structure.
- 4.53** Finally, although the 'ratings shopping' concerns that arose for CRAs are perhaps less acute in the case of ESG ratings, the profile of particular providers' ratings could influence both issuers' decisions as to which provider's questionnaires to respond to, and investors' decisions as to which provider's ratings to reference in its investment processes, contracts or indices.

**Table 1: Comparison of policy issues for credit rating agencies and ESG rating providers**

Policy issues and underlying problems <sup>2</sup>	Credit rating agencies (CRAs)	ESG rating providers
Unreliable ratings <ul style="list-style-type: none"> <li>Methodological issues and model risk</li> </ul>	<ul style="list-style-type: none"> <li>Following the 2008-09 financial crisis, CRAs were criticised for alleged methodological failures, particularly in the structured finance sector (see Issing, 2008). Concerns were also raised about CRAs' ability to recruit and retain skilled analysts, about their slowness to react to new information, and their reliance on low-quality data inputs.</li> </ul>	<ul style="list-style-type: none"> <li>Without good transparency of rating methodologies, it is difficult to verify the appropriateness of the providers' methodologies. This includes their choices about which ESG attributes to consider, how to measure performance on these attributes, how to weigh different attributes in forming a rating, and how to deal with incomplete and unreliable data inputs.</li> </ul>

2 These issues are as set out in Deb et al. (2011)

Policy issues and underlying problems <sup>2</sup>	Credit rating agencies (CRAs)	ESG rating providers
<p>Bias in ratings</p> <ul style="list-style-type: none"> <li>Conflicts of interest and ratings shopping</li> </ul>	<ul style="list-style-type: none"> <li>CRAs generally operate an 'issuer pays' model, in which revenues derive predominantly from fees from rated borrowers. This business model introduces inherent conflicts of interest where the CRAs may be incentivised to issue higher ratings in order to gain or retain existing business</li> <li>Similarly, there were concerns that issuers were engaging in 'ratings shopping' – selecting a rating provider based on the highest achievable rating.</li> <li>There have also been concerns that the potentially systemic consequences of hardwiring (see below) could make CRAs more cautious about rating downgrades, leading to an upward bias in ratings.</li> </ul>	<ul style="list-style-type: none"> <li>ESG rating providers typically operate an 'investor pays' model, in which investors and other market participants pay a subscription. While this model reduces the potential for conflicts, such conflicts could still arise when rating a related party.</li> <li>Ratings shopping may be a less direct concern for 'investor pays' ESG ratings. However, the provider's methodology and its implications for ratings could influence which providers' questionnaires an issuer chooses to respond to. The profile of a provider's ratings could also bias which provider an asset manager chooses to reference in its investment processes, contracts or indices.</li> <li>There is also a concern that, as ESG ratings are increasingly relied upon within investment processes and contracts, ESG rating providers may have an incentive to build more rigidity into their rating methodologies in order to avoid systemic effects.</li> </ul>

Policy issues and underlying problems <sup>2</sup>	Credit rating agencies (CRAs)	ESG rating providers
<p>Cliff-edge effects, over-reliance and adverse incentives</p> <ul style="list-style-type: none"> <li>a. Hardwiring and mechanistic reliance</li> <li>b. Lack of diversity in ratings</li> <li>c. Misperception of what ratings represent</li> </ul>	<ul style="list-style-type: none"> <li>a. Credit ratings are referenced in firms' investment processes and in a wide range of financial contracts. They are also used for regulatory purposes in many jurisdictions – for instance, to calculate regulatory capital requirements for banks and insurers. Rating changes – especially downgrades that drop to sub-investment grade – can therefore have systemic effects.</li> <li>b. The largest three CRAs have a market share of around 95% in the EU. The correlation between the leading CRAs' ratings is estimated to be around 0.98.</li> <li>c. With insufficient transparency of CRAs' methodologies prior to the introduction of regulation, many users may not have fully understood what the ratings represented.</li> </ul>	<ul style="list-style-type: none"> <li>a. ESG ratings are increasingly referenced in firms' investment processes and in contracts and indices underpinning investment products/services. This could eventually lead to market-wide effects arising from rating changes – eg, as certain issuers are excluded from indices. Given the variability in ratings among providers, the choice of provider to reference in investment processes, contracts or indices could also have significant implications for the allocation of capital.</li> <li>b. The correlation between providers' ratings is low. While such diversity can be beneficial, this can have adverse consequences if users cannot adequately observe and interpret the sources of divergence.</li> <li>c. In the absence of a common ESG framework, ESG ratings may be difficult to interpret. Furthermore, given the multi-dimensionality of ESG ratings, the lack of transparency of providers' methodologies makes it difficult to understand what ratings represent, and to interpret both rating changes and differences in ratings across providers.</li> </ul>

**4.54** A number of different policy actions could be considered to address the potential harms on both the demand and the supply side of ESG rating provision. Some of these may also be relevant to other types of ESG data provider. These range from regulatory guidance for users of ratings, to 'soft' regulation of ratings provision, to the introduction of a formal regulatory framework for ESG ratings:

- **Guidance for firms on their use of third-party ESG data and ratings** – develop guidance on existing Handbook requirements to enhance risk management processes supporting the use of ESG ratings and other third-party ESG data, reiterating expectations around the management of outsourcing arrangements, due diligence and the use of ratings in benchmarks and indices
- **Best Practice Code for ESG data and rating providers** – encourage voluntary, industry-led adherence to minimum conduct standards in areas such as transparency, governance and management of conflicts of interest
- **Regulation of ESG data and rating providers** – work with the Treasury to bring ESG ratings within the regulatory perimeter, as has been suggested in the EU by ESMA, and the AMF and AFM. Again, such a regime might focus primarily on transparency, governance and management of conflicts of interest



**4.55** Consideration of the regulation of ESG data and rating providers is still emerging, with the EU the main jurisdiction actively contemplating such intervention.

**4.56** Given the very different nature of the services provided by the various different types of ESG data and rating providers, it may be appropriate to consider the case for – and nature of – regulatory intervention separately for the different types of service provider.

**4.57** Since ESG rating providers operate and cover companies globally, we consider that there would be a strong benefit in a globally applicable regulatory approach, rather than a local regime. However, global coordination can often take time and the harms may arise locally in the meantime.

**4.58** We welcome your views on the issues raised in this section.

**Q17:** 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?

**Q18:** 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?

**Q19:** 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.

**Q20:** 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
- 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



## Sustainable finance in wider capital markets

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- 4.59** We acknowledge that the issues we have focussed on in this discussion chapter are by no means exhaustive of relevant ESG issues in capital markets.
- 4.60** We note for instance, topical issues around including ESG principles in the securities lending market, developing carbon offset markets, and embedding sustainability considerations more fully in commodities markets.
- 4.61** While we have started to engage with market participants on these and other topics, we welcome views on areas that we should be prioritising to support our strategic objective to make relevant markets function well.

**Q21:** What other ESG topics do you consider that we should be prioritising to support our strategic objective? Please explain.

## Annex 1

### Questions in this paper

#### Consultation paper

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- Q1:** 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?
- Q2:** 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?
- Q3:** 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?
  - d.** Are there any other matters we should take into consideration – eg, competitiveness, complexity of the application of the rule, burden on issuers in LR 17, or the feasibility to comply with any potential rules?

- Q4:** 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?
- Q5:** 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
  - b.** the TCFD's proposed standalone guidance document on metrics, targets and transition planning
  - c.** the TCFD's technical supplement on measuring portfolio alignment.
- If not, what alternative approach would you prefer?
- Q6:** Do you agree that we should update the Technical Note 801.1 to reflect the proposed new rule and associated guidance in this CP?
- Q7:** 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.
- Q8:** 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?
- Q9:** 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?
- Q10:** Do you agree that our new rule should take effect for accounting periods beginning on or after 1 January 2022? If you consider that we should set a different timeframe, please explain why.
- Q11:** Do you agree with the conclusions and analysis set out in our cost benefit analysis (Annex 2)?

## Discussion Chapter

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- Q12:** 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?
- Q13:** Should the FCA explore supporting the UoP bond market by recognising existing standards (eg, ICMA Principles), potentially through our recognition of industry codes criteria and process?
- Q14:** 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
- Q15:** We would welcome views on the potential harm set out above and what, if any, actions the FCA or the Treasury should consider.
- Q16:** Should the FCA, alongside the Treasury, consider the development and creation of a UK bond standard, starting with green bonds?
- Q17:** 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?
- Q18:** 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?
- Q19:** 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.
- Q20:** 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
- 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

**Q21:** What other ESG topics do you consider that we should be prioritising to support our strategic objective? Please explain.

## Annex 2

# Cost benefit analysis

### Introduction

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1. FSMA, as amended by the Financial Services Act 2012, requires us to publish a cost benefit analysis (CBA) of our proposed rules. Specifically, section 138I requires us to publish a CBA of proposed rules, defined as 'an analysis of the costs, together with an analysis of the benefits that will arise if the proposed rules are made'.
2. This analysis presents estimates of the significant impacts of our proposal. We provide monetary values for the impacts where we believe it is reasonably practicable to do so. For others, we provide estimates of outcomes in other dimensions. Our proposals are based on carefully weighing up these multiple dimensions and reaching a judgement about the appropriate level of consumer protection, taking into account all the other impacts we foresee.

### Our analytical approach

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3. To understand the impact of the proposed rule change set out in Chapter 3, this CBA considers:
  - the likely compliance costs to in-scope issuers,
  - the likely benefits to issuers and the wider market.
4. As a regulator, we will also incur costs from supervising against the new rules. We will assess the resource implications as part of our annual business planning.
5. The analysis presented below has been produced using evidence from the following sources:
  - A study completed by a team at the London School of Economics (LSE) examining the current status of premium listed issuers' climate-related disclosures.<sup>3</sup> Findings from this research were used to support the analysis for the cost benefit analysis in CP20/3.
  - Reports on the current status of climate-related disclosures and other non-financial reporting published by the [FRC](#), the [TCFD](#), [KPMG](#) and [ClientEarth](#), as referenced in Chapter 2.
  - Engagement with industry on the challenges in effectively reporting against the TCFD recommendations

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<sup>3</sup> This work was carried out as an FCA-supported project in 2019. The FCA specified the aim of the project and engaged frequently with the group for the duration of the work.

## Problem and rationale for intervention

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6. We describe the problem and rationale for intervention in Chapters 1 and 2, noting that this proposal extends the application of the existing Listing Rule (LR 9.8.6(8)R) for commercial companies with a UK premium listing to a wider set of listed issuers.
7. We further note that there is evidence that many listed companies – including those that are subject to, but have not yet made disclosures in line with, LR 9.8.6(8)R, and those with a standard listing that are not within the scope of LR 9 – are not yet making sufficient climate-related disclosures that provide markets with the information they need to make informed business, risk and investment decisions.
8. As set out in Chapter 1, if issuers' disclosures of climate-related risks and opportunities are insufficient, assets could be mispriced and capital misallocated. Issuers themselves may also face harms if they are unable to access financial markets at a cost of capital that appropriately reflects their management of climate-related risks and opportunities. We also describe consequential harms that might arise for consumers of financial products.
9. We consider that these harms arise from market failures, which include:
  - **Asymmetric information.** A lack of visibility of issuers' climate-related exposures to investors reflects, at its core, the principal-agent problem that arises where there is a separation of ownership and control. Issuers may voluntarily disclose less than investors might prefer, due to the coordination failures mentioned below, and the cost of making extensive disclosures. Directors may also have concerns about legal liability for forward-looking projections or the commercial sensitivity of disclosed information.
  - **Coordination failure among issuers.** An issuer may have a disincentive to be a 'first-mover' in making voluntary disclosures. They may fear reputational damage or an adverse market response if they are perceived not to have invested sufficiently to manage the impacts of climate change.
  - **Coordination failure among investors.** Investors may be unable to coordinate effectively to encourage a market-led improvement in climate-related disclosures across issuers. Issuers' disclosures will then be determined by their own private incentives.
10. The causal chain set out in Chapter 1 (Figure 1) shows how by extending the application of our TCFD-aligned disclosure requirements to issuers of standard listed equity shares, we expect to advance our objectives in respect of market integrity and consumer protection, and mitigate the harms described above.

## Baseline and key assumptions

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11. To establish the baseline for the CBA, we assume that without our intervention disclosures by issuers of standard listed equity shares would not cover the TCFD's recommendations and recommended disclosures.
12. In assessing the impact of this proposal, we have also taken a broadly similar approach to that in our CBA for our Listing Rule for premium listed companies in CP 20/3. Responses to the CBA in CP 20/3 were generally supportive of our analysis.

13. Our proposals will apply to around 148 issuers of standard listed equity shares. The size of listed companies was determined using information on their market capitalisation values. We have excluded standard listed investment entities and shell companies, reflecting the scope of our proposed rules.

### Summary of proposals

14. Our proposals are set out in Chapter 3. We propose to introduce a new rule in LR 14, extending the application of the disclosure rule in LR 9.8.6(8)R, which references the recommendations and recommended disclosures in the TCFD's final report, as published in June 2017.
15. Our proposed rule will apply to issuers of standard listed equity shares (excluding standard listed investment entities and shell companies). Under our proposal, the rule will be introduced, at least initially, on a 'comply or explain' basis.

### The current status of issuers' climate-related disclosures

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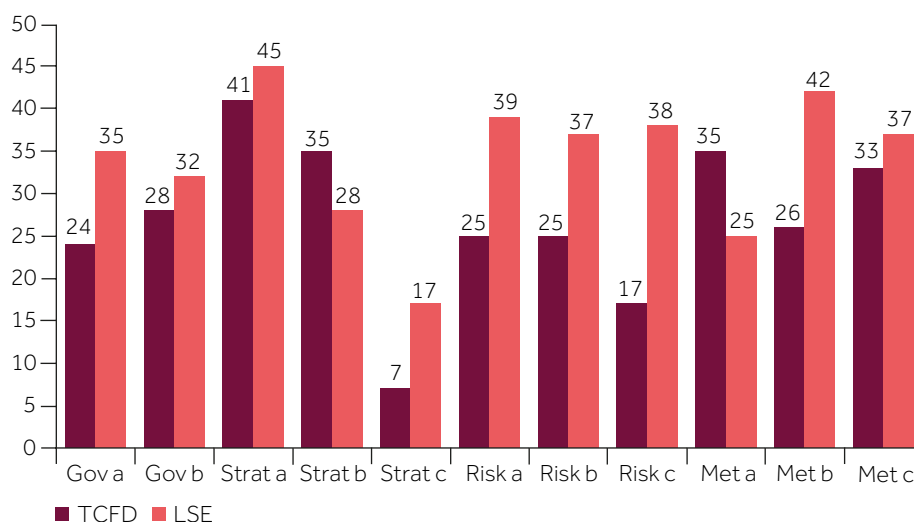
16. A number of existing obligations, including under the Companies Act, require directors, as stewards, to consider carefully all factors that could be material to their companies' prospects. This will include climate-related factors.
17. However:
- Existing disclosure obligations do not cover the full scope of disclosures contemplated by the TCFD's recommendations and do not specify a consistent form or structure for these disclosures.
  - Even where companies have established governance, strategy and risk management arrangements that help directors to assess climate-related impacts on their businesses, they often do not fully describe the nature and scope of these arrangements in their disclosures. This may reflect the incentives and coordination failures described above.
18. The supporting analysis for the CBA in CP20/3 is still particularly relevant to how we gauged the current market practice. The LSE's study of existing climate-related disclosures provided us with a baseline for the calculation of costs for our CBA for premium listed commercial companies.
19. Listed companies have continued to make progress in building relevant capabilities and enhancing their climate-related disclosures since the LSE's study was carried out. However, other evidence (including from the FRC, the TCFD, KPMG and ClientEarth) suggests that there remains considerable variability in existing climate-related disclosures. In the TCFD's 2020 Status Report (which is a global study), there were increases in the proportion of companies reporting against the majority of the 11 recommended disclosures, but the average increase was just 3%.
20. Accordingly, we consider that the baseline of the LSE's study remains a reasonable baseline for the readiness of the larger standard listed companies. Therefore, based on the LSE study presented in CP 20/3, Figure 5 below presents an estimate of the



assumed baseline percentage of larger in-scope issuers of standard listed equity shares that are already making disclosures consistent with each recommended disclosure in their public reports.<sup>4</sup>

21. As a point of reference, we compare the disclosure data for the sample of premium listed issuers with global results presented in the TCFD's 2020 Status Report. In most cases, the findings in the LSE study are broadly consistent with those in the TCFD's global sample.

**Figure 5: The percentage of companies making TCFD-aligned disclosures**



Note: Gov a – board oversight; Gov b – management role; Strat a – identified climate-related risks and opportunities; Strat b – resilience of strategy/scenario analysis; Risk a – identifying climate risks; Risk b – managing climate risks; Risk c – integration of climate risk management; Met a – metrics applied; Met b – Scope 1, 2 and (if appropriate) 3 emissions; Met c – targets.

Source: TCFD Status Report, October 2020; LSE; the values depicted in the figure are the percentages of companies in each study making disclosures aligned with each of the 11 recommended disclosures, as introduced in Appendix 3. In the case of the LSE study, the value presented is an average across all of the disclosure items mapped to that recommended disclosure. We note that there have been methodological changes to the TCFD's analysis, which make it difficult to compare directly the findings in the 2020 Status Report with those in the 2019 Status Report.

22. Two of the most challenging areas of disclosure among issuers continue to be:
- climate scenario analysis to assess the resilience of the organisation's strategy – Strategy (c),
  - disclosure of business-relevant climate metrics and targets – Metrics and Targets (a) and (c).
23. This finding is broadly consistent with evidence in other studies and reports, including those by the FRC, as well as our liaison with issuers and other stakeholders.
24. As noted in Chapter 3, standard listed issuers of equity shares are, on average, smaller in size, by market capitalisation, than premium listed companies (see Figure 2). Our stakeholder engagement indicates that climate-related disclosures of smaller

4 For each disclosure item, we calculate the number of issuers that include that item in their public reports. We then sum the scores for all disclosure items mapped to a particular recommended disclosure and divide by the number of mapped disclosure items. This gives us the average number of issuers that disclose each mapped disclosure item. Expressed as a percentage, this is our estimate of the percentage of issuers that disclose in line with that recommended disclosure.

standard listed companies' are less mature than those of premium listed companies. ClientEarth similarly found that companies with a smaller market capitalisation have typically made less progress in making relevant climate-related disclosures.

25. Consistent with our Handbook Glossary definition that applies in MAR 5, we define small and medium-sized (SME) issuers of standard listed equity shares as companies with a market capitalisation below €200 million. We conservatively estimate that SME issuers of standard listed equity shares have not yet begun to make the necessary investments in climate-related disclosure capabilities. Consequently we assume that *all* of these companies will incur up-front costs of compliance.

## Summary of costs and benefits

26. Compliance costs to in-scope issuers of standard listed equity shares are estimated in Table 2 below. We believe that listed companies will incur compliance costs only as a direct result of the proposed disclosure requirements. Therefore, the reported figures do not include any costs resulting from any market impact arising from the intervention (eg, changes to business models, product prices, or market exit).

**Table 2: Estimated compliance costs to issuers**

Category of cost	No. of impacted issuers	One-off cost (£m)	Ongoing cost (£m, p.a.)
<i>Familiarisation and legal review</i>	148	1.8	N/A
<i>Coordination of disclosure inputs across functions</i>	95	15.4	7.3
<i>Scenario analysis (Strategy (c))</i>	129	7.8	3.9
<i>Metrics/Targets (a), (c)</i>	102	9.3	4.6
<i>Metrics/Targets (b)</i>	86	4.3	
<b>Total</b>		<b>38.6</b>	<b>15.8</b>

27. We do not consider that it is reasonably practicable to quantify the benefits of our proposals. We have therefore not sought to quantify the benefits to the market from reducing the identified harms. Instead we have estimated the minimum net benefit required in order to justify the intervention.
28. In particular since the estimated costs of compliance are small relative to market capitalisation, even a small improvement in price efficiency flowing from these benefits would be sufficient to outweigh the cost and produce a net benefit.
29. The remainder of this section describes in more detail the approach we have taken and the assumptions that we have made.

## Calculating compliance costs

30. Our proposed rules will impact the 148 commercial companies that are currently admitted to the Official List and are issuers of standard listed equity shares. These companies comprise around 30% of the total market capitalisation of the LSE Main Market.

31. A breakdown of in-scope companies by size and sector is introduced in Chapter 3. In-scope issuers include a wide variety of companies, headquartered in the UK and abroad. There is also a significant range in the market capitalisations of the companies, with the 10th percentile company having a market capitalisation of £4.5 million compared to the 90th percentile company having a market capitalisation of £16.2 billion.

### **Sources of incremental costs**

32. Based on our analysis of the current status of disclosures, we consider the following to be the key areas in which incremental costs of compliance will be incurred:
- **Coordination of inputs.** Successful implementation of the TCFD's recommendations will require a multi-disciplinary approach. According to engagement with a number of issuers, such an approach is likely to entail coordination of inputs from across various functions in the organisation (eg, finance, legal, risk), as well as integration of climate reporting with existing reporting and governance arrangements.
  - **Climate scenario analysis (Strategy (c)).** This is the least developed area of disclosure and we expect that most issuers will need to make initial investments to build their capabilities.
  - **Climate metrics and targets** (Metrics and Targets (a) and (c)). We expect that many issuers will also need to make initial investments to enhance their capability to monitor a range of business-relevant climate-related metrics.
  - **Scope 1 and 2 emissions** (Metrics and Targets (b)). While some UK regulations require disclosures in this area already, some issuers are likely to need to enhance these, in particular those overseas headquartered companies who may not face similar disclosure requirements in their home jurisdictions.
33. Issuers will incur one-off costs to enhance their disclosures to ensure that they are consistent with the TCFD's recommendations in each of these areas. In addition, issuers will incur one-off costs in familiarising themselves with our proposed new rule and the various TCFD's publications referenced in the proposed rule and associated guidance.
34. In building their capabilities, issuers will be able to draw on the growing body of guidance and tools to support implementation of these recommended disclosures.
35. Once issuers have built capabilities across all of the recommended disclosures, they will continue to incur some costs to support their coordination, information management and reporting activities on an ongoing basis. Furthermore, as industry know-how and data availability improve and issuers' own capabilities evolve, we anticipate that issuers will make further enhancements to their disclosures.

### **Assumptions**

36. To better understand the types of one-off and ongoing incremental costs associated with implementing the recommendations, we have considered the information we collected when preparing the CBA for CP20/3, as well as the feedback received to CP 20/3 and ongoing discussions with industry. For the purposes of our CBA, we have made several assumptions:
- **Resourcing.** We assume that the main source of incremental costs is the cost of hiring or reallocating staff resources to coordinate inputs and develop capabilities. We recognise that there are various approaches that issuers may wish to take to comply with our proposed rules. For instance depending on their existing resources, capabilities and access to data, some issuers may hire new staff or reallocate existing staff and

other resources, while others may rely more heavily on external consultants. Our assumptions constitute just one possible approach.

- **Source data.** We have not included incremental data sourcing costs, as data needs will differ by issuer, by sector, and by chosen metric and scenario analysis methodology. It is therefore not practicable to estimate these costs. We recognise that access to some relevant data is likely to be challenging, at least initially. Some issuers may choose to subscribe to data services to facilitate access to these public sources and many issuers already do so. However, many data items are likely to be available from public sources – including from Government and non-Government organisations. The completeness of data to support issuers' analysis is likely to improve over time.
- **Board engagement.** We also recognise that companies' boards and executive management are likely to need to engage in climate-related issues more deeply. They will also need to invest more time in reviewing and challenging the issuer's climate-related disclosures once produced. We have not specifically quantified and attributed this as a compliance cost. As climate-related risks and opportunities become more material, we consider that enhancing board engagement on these issues will be integral to directors' role as good stewards of their businesses. We therefore consider that this is something directors will increasingly need to do under existing Companies Act expectations, irrespective of our proposed new rule. We do not therefore consider that this should be regarded as a cost directly attributable to our proposals.
- **Issuer characteristics.** As described in Chapter 3, issuers of standard listed equity shares vary in size, sector and complexity of business. We recognise that the cost of compliance may depend on these factors at least in part – including, for instance, the characteristics of the issuer's fixed asset base, its cross-border operations and its supply chain. However, we do not have sufficient credible information to quantify compliance costs along these dimensions. In this analysis, we have used 'size' as a proxy and estimated an average cost of compliance for each of two size groups, defined by their market capitalisation: larger in-scope issuers; and SMEs.

**37.** As noted, there is a substantial difference in the size profile of standard listed companies, relative to premium listed companies, with 13% of the latter valued below €200 million in market capitalisation as of 31 May 2021<sup>5</sup>, compared with nearly two thirds of in-scope standard listed companies. We expect that SMEs have less complex businesses, such that they might find it easier to identify, measure and report sources of climate-related risks and opportunities. However, we acknowledge that, while lower in absolute terms, the costs of compliance for SMEs may be higher as a proportion of revenues or market capitalisation than in the case of larger companies.

**38.** Recognising the need for a proportionate approach to implementation of our rule, we note the principles-based nature of the TCFD's recommendations. We also note our proposed guidance (see paragraph 3.31), which sets out that, in determining the appropriate level of detail to include in its disclosures, a listed company should take account of factors such as the level of its exposure to climate-related risks and opportunities and the scope and objectives of its climate-related strategy. These factors may be related to the nature, size and complexity of the business.

**39.** On the basis of the above, we assume that compliance costs in several categories will be lower for SME issuers by a factor between 0–50%, with an average cost reduction of 25%. Specifically, we assume that SMEs will incur 25% lower costs across the following cost categories: (i) coordination of inputs; (ii) climate scenario analysis; (iii) climate metrics and targets; (iv) scope 1 and 2 emissions. We have applied these cost

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5 Based on the Instrument list data obtained from the [London Stock Exchange](#).

reductions by lowering the assumed FTE resources required under the various cost categories, doing so in respect of both one-off and ongoing costs.

- 40.** As noted in paragraph 25, we also assume that SMEs will not yet have made any investment in the capabilities requirement to make climate-related disclosures aligned with the TCFD's recommendations. Accordingly, while we assume that some proportion of larger in-scope companies will already be making disclosures and hence will not incur incremental costs (informed by the LSE study), our cost estimates are applied to *all* SME issuers.
- 41.** Among 148 in-scope issuers, the market capitalisation of 87 companies was below the threshold defined in paragraph 25.
- Calculating one-off costs**
- 42.** Reflecting these assumptions, Table 3 summarises how we calculated the initial one-off compliance costs to issuers for the first year.
- 43.** For each category of cost, we have adjusted the number of impacted larger issuers to account for those that are likely already making relevant disclosures aligned with the TCFD's recommendations. That is, for each category of cost, the number of larger issuers impacted is calculated as the total number of in-scope larger issuers (61) multiplied by the average proportion of issuers that are not already making disclosures aligned with the recommended disclosures relevant to that category of cost (according to the outcome of the LSE study presented in Figure 5). For example, for scenario analysis (Strategy (c)), below, the number of issuers impacted is calculated as:  $(1-0.17) \times 61 = 51$ . As noted, for SMEs we apply the cost to all issuers.
- 44.** In our estimation of compliance costs we have used the Standardised Cost Model as set out in our approach to CBAs.

**Table 3: Calculation of the initial one-off compliance costs**

Category of cost	Estimation methodology	Total
<b>Familiarisation and legal review costs</b>	<p>Assume two compliance/regulatory analysis staff review the consultation paper to familiarise themselves with the proposals and two legal/regulatory analysis staff review the legal text in annex and the relevant TCFD documents.</p> <p>Staff costs for this review are calculated according to our Standard Cost Model<sup>6</sup>:</p> <ul style="list-style-type: none"> <li>Approximately 3 hours for each compliance/ regulatory analysis staff member to review the consultation paper (based on the size of the document) at an hourly-equivalent salary of £63,</li> <li>86 hours for each legal/regulatory analysis staff member to review the legal text and the relevant TCFD documents (based on the size of the documents) at an hourly-equivalent salary of £69.</li> </ul> <p>In summary, we calculate these staff costs as: <math>148 \times [(2 \times 3 \times 63) + (2 \times 86 \times 69)]</math>. We take an analogous approach for all other cost categories.</p> <p>Total number of impacted issuers: <b>148</b></p>	<p>Average for a single issuer: <b>£12,246</b></p> <p>Average for the industry: <b>£1,812,408</b></p>

<sup>6</sup> In applying our Standard Cost Model we have applied relevant salary estimates for medium-sized companies to all 148 companies. We have done this for simplicity and there is little difference in the salary estimates for the relevant functions between SME and larger companies. Using different estimates would not significantly change the assessment in our cost benefit analysis.

Category of cost	Estimation methodology	Total
<b>Coordination of disclosure inputs across functions</b> <i>relevant recommended disclosures: Governance (a) and (b), Strategy (a) and (b), and Risk Management (a)-(c)</i>	<p>Based on our discussions with a cross-section of issuers to support the CBA for premium listed issuers in CP20/3, we have made assumptions about the approach to coordinating inputs from across the organisation to inform recommended disclosures on governance, strategy and risk management.</p> <p>The issuers we spoke to typically allocated central responsibility to a small team of people and established some mechanism for multi-disciplinary input. While the issuers consulted were unable to quantify the proportion of time allocated by functional specialists across the organisation, our assumptions are consistent with the qualitative input received:</p> <ul style="list-style-type: none"> <li>two FTEs for larger issuers or 1.5 FTE for SME issuers (in the Finance Department) are responsible for developing the approach to disclosures, coordinating inputs across the organisation and preparing the disclosures; annual salary costs for these individuals are estimated as £52,790<sup>7</sup></li> <li>inputs are sought from the following functions: Strategy; Finance; Risk; Reporting; Company Secretariat; Sustainability; Investment Relations; Senior Management</li> <li>the issuer establishes a cross-functional Working Group consisting of 8 specialists, if the issuer is large, or of 6 specialists, if the issuer is an SME, with representatives of each of the functions listed above; the working group agrees a joined-up strategic approach to disclosure across the organisation</li> <li>each member of the Working Group allocates 5% of time to TCFD disclosures in the first year; annual salary costs are estimated here as 0.05 x £105,983 (based on the average senior manager, all functions, salary in our Standard Cost Model).</li> </ul> <p>Number of larger impacted issuers: 39</p> <p>Number of SME impacted issuers: 87</p> <p>Total number of impacted issuers: <b>126</b></p>	<p>Average for larger issuer: <b>£147,973</b></p> <p>Average for SME issuer: <b>£110,980</b></p> <p>Average for the industry: <b>£15,426,206</b></p>
<b>Scenario analysis</b> <i>relevant recommended disclosures: Strategy (c)</i>	<p>We assume that:</p> <ul style="list-style-type: none"> <li>the larger issuer appoints one FTE and the SME issuer appoints between a half and one full FTE<sup>8</sup> of a quantitative analyst to: develop a scenario analysis methodology tailored to the circumstances of the business, source relevant data, and build a systems capability to support systematic analysis and reporting</li> <li>annual salary costs are estimated here at £65,791.<sup>9</sup></li> </ul> <p>Number of larger impacted issuers: 53</p> <p>Number of SME impacted issuers: 87</p> <p>Number of impacted issuers: <b>140</b></p>	<p>Average for larger issuer: <b>£65,791</b></p> <p>Average for SME issuer: <b>£49,343</b></p> <p>Average for the industry: <b>£7,779,786</b></p>

7 This estimate is based on a review of representative salaries across vacancies for Finance Manager roles on online platforms.

8 For all intervals mentioned in the context of SME firms' FTE requirements in this table, we used interval midpoints for calculations.

9 This estimate is based on a review of representative salaries across vacancies for quantitative analyst roles in the UK on online platforms.

Category of cost	Estimation methodology	Total
<b>Metrics/Targets</b> <i>relevant recommended disclosures: Metrics and Targets, (a) and (c)</i>	<p>Again, based on qualitative input from discussions with a cross-section of issuers we assume that:</p> <ul style="list-style-type: none"> <li>the larger issuer appoints one FTE and the SME issuer appoints between 0.5 to 0.75 FTE of a risk/sustainability analyst to develop a set of business-relevant metrics and targets, source relevant data, and build a systems capability to support systematic analysis and reporting</li> <li>annual salary costs are estimated here at £86,518 (based on the average risk management salary in our Standard Cost Model).</li> </ul> <p>Number of larger impacted issuers: 42  Number of SME impacted issuers: 87  Number of impacted issuers: <b>129</b></p>	<p>Average for larger issuer: <b>£86,518</b>  Average for SME issuer: <b>£64,889</b>  Average for the industry: <b>£9,279,056</b></p>
<b>Metrics/Targets – Scope 1 and 2 emissions</b> <i>relevant recommended disclosures: Metrics and Targets, (a) and (c)</i>	<p>Again, based on qualitative input from discussions with a cross-section of issuers, we assume that:</p> <ul style="list-style-type: none"> <li>the larger issuer appoints 0.5 FTE and the SME issuer appoints between 0.25 and 0.5 FTE of a risk/sustainability analyst to enhance its disclosures of Scope 1 and 2 emissions; the annual salary costs are estimated here at £86,518 (based on the average annual risk management salary in our Standard Cost Model).</li> </ul> <p>Number of larger impacted issuers: 35  Number of SME impacted issuers: 87  Number of impacted issuers: <b>122</b></p>	<p>Average for larger issuer: <b>£43,259</b>  Average for SME issuer: <b>£32,444</b>  Average for the industry: <b>£4,336,715</b></p>
<i>Total one-off cost for the <b>larger issuer</b></i>		<b>£355,787</b>
<i>Total one-off cost for the <b>SME issuer</b></i>		<b>£269,902</b>
<b>Total one-off cost for the industry</b>		<b>£38,634,170</b>

### Calculating ongoing costs

45. Table 4 summarises how we calculated the ongoing compliance costs to issuers. Our baseline assumption is that those issuers that are currently already disclosing voluntarily would have continued to do so even in the absence of our proposed new rules. Accordingly, we apply the same assumptions as above in respect of the number of impacted issuers for each category of cost.
46. Our assumptions are based on our discussions to support the CBA in CP20/3 with a subset of issuers and follow the assumptions in Table 3 on the necessary skillsets and the arrangements an issuer may put in place to gather multi-disciplinary input. For each category of cost however, we scale back the resource requirement on the basis that fewer resources are likely to be required on an ongoing basis to evolve the organisation's capabilities and approach and prepare the disclosures.



**Table 4: Calculation of the ongoing compliance costs**

Category of cost	Estimation methodology	Total
<b>Coordination of disclosure inputs across functions</b>	<p>We assume that:</p> <ul style="list-style-type: none"> <li>one FTE at the larger issuer and between half and one FTE<sup>10</sup> at the SME issuer (in either the Finance or Sustainability Department) remain responsible for evolving the approach to disclosures, coordinating inputs across the organisation, and preparing the disclosures; as before, annual salary costs are estimated here at £52,790</li> <li>on an ongoing basis, the cross-functional Working Group, consisting of 8 members at the larger issuer and 6 members at the SME issuer, allocates 2% of time to TCFD disclosures after the first year; salary costs for each member are estimated as 0.02 x £105,983 (based on the average senior manager, all functions, salary in our Standard Cost Model).</li> </ul> <p>Number of larger impacted issuers: 39</p> <p>Number of SME impacted issuers: 87</p> <p>Total number of impacted issuers: <b>126</b></p>	<p>Average for larger issuer: <b>£69,747</b></p> <p>Average for SME issuer: <b>£52,310</b></p> <p>Average for the industry: <b>£7,271,154</b></p>
<b>Scenario analysis relevant recommended disclosures: Strategy (c)</b>	<p>We assume that:</p> <ul style="list-style-type: none"> <li>the larger issuer allocates 0.5 FTE and the SME issuer allocates between 0.25 and 0.5 FTE of a quantitative analyst to evolve the approach to scenario analysis and run the scenarios to feed into ongoing disclosures; annual salary costs are estimated at £65,791.<sup>11</sup></li> </ul> <p>Number of larger impacted issuers: 53</p> <p>Number of SME impacted issuers: 87</p> <p>Total number of impacted issuers: <b>140</b></p>	<p>Average for larger issuer: <b>£32,896</b></p> <p>Average for SME issuer: <b>£24,672</b></p> <p>Average for the industry: <b>£3,889,893</b></p>
<b>Metrics/Targets relevant recommended disclosures: Metrics and Targets, (a), (b) and (c)</b>	<p>We assume that:</p> <ul style="list-style-type: none"> <li>the larger issuer allocates 0.5 FTE and the SME issuer allocates between 0.25 and 0.5 FTE of a risk/sustainability analyst to manage the ongoing compilation and reporting of all business-relevant metrics (including those under Metrics and Targets (b)) and evolve the approach to setting targets; annual salary costs are estimated at £86,518 (based on the average risk management salary in our Standard Cost Model).</li> </ul> <p>Number of larger impacted issuers: 42</p> <p>Number of SME impacted issuers: 87</p> <p>Total number of impacted issuers: <b>129</b></p> <p>(based on the number of issuers impacted by Metrics and Targets (a) and (c))</p>	<p>Average for larger issuer: <b>£43,259</b></p> <p>Average for SME issuer: <b>£32,444</b></p> <p>Average for the industry: <b>£4,639,528</b></p>
<b>Total ongoing cost for the larger issuer</b>		<b>£145,902</b>
<b>Total ongoing cost for the SME issuer</b>		<b>£109,426</b>
<b>Total ongoing cost for the industry</b>		<b>£15,800,575</b>

## Benefits to issuers and the wider market

47. We do not consider that it is reasonably practicable to quantify the benefits of our proposals. As described in our causal chain analysis, by their nature, many of the benefits will be indirect, accruing from better market functioning.

10 For all intervals mentioned in the context of medium-sized firms' FTE requirements in this table, we used interval midpoints for calculations.

11 This estimate is based on a review of representative salaries across vacancies for quantitative analyst roles in the UK on online platforms.



48. We have therefore not sought to quantify the benefits to the market from reducing the identified harms. Instead we have estimated the minimum net benefit required in order to justify the intervention.

### **Sources of benefits**

49. The benefits arising from our intervention are illustrated in the causal chain set out in Figure 1.
50. The benefits accrue from better-informed decision making both within companies (due to more systematic consideration of climate-related risks and opportunities) and in financial markets. We believe that this will lead to improved market functioning and market access for issuers at a cost of capital that more appropriately reflects their management of climate-related risks and opportunities.
51. The finance literature identifies a number of benefits to the efficiency of asset pricing arising from public disclosure of information relevant to investment decisions. There is also academic evidence in support of the notion that better transparency lowers the cost of capital.<sup>12</sup> We also note that the financial impacts of climate-related risks and opportunities are relevant to all issuers, and likely to be material for many of them.
52. There is also some evidence that issuers increasingly see material private benefits to improving their own climate-related disclosures – including from enhancing their reputation and proactively meeting investors' demands for information. This was the message in a survey of board members of some of the UK's largest companies published by the Carbon Trust in January 2019. The survey was conducted by Ipsos Mori as part of its annual Captains of Industry research study. Around a third of companies perceived a positive financial impact from improving their disclosures, arising from factors such as improved access to capital, a lower cost of capital and a stronger credit rating.
53. More generally, benefits are expected to accrue to the market and to society through better allocation of capital and a smoother and faster transition to a zero-carbon economy.

### **Estimating the minimum net benefit required**

54. The total one-off compliance cost of £38.6 million equates to 0.004% of the £974.2 billion total market capitalisation of in-scope issuers of standard listed equity shares. Similarly, the total ongoing annual compliance cost of £15.8 million equates 0.002% of the total market capitalisation of in-scope issuers. Since the estimated costs of compliance are small relative to market capitalisation, even only a small improvement in price efficiency flowing from these benefits would be sufficient to outweigh the cost and produce a net benefit.
55. However the benefits might reasonably be expected *substantially* to exceed the costs of compliance if more informed asset pricing encourages capital flows to companies which manage climate related risks and opportunities more effectively. If this occurs, the likelihood that the more severe projections of the economic and social costs of climate warming materialise may decrease.

12 Barth, Konchitchi and Landsman (2013), Cost of capital and earnings transparency, *Journal of Accounting and Economics*; Lang and Maffett (2010), Economic effects of transparency in international equity markets: A review and suggestions for future research, *Foundation and Trends in Accounting*, Vol 5, No. 3, pp175-241.

## Annex 3

# Compatibility statement

### Compliance with legal requirements

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1. This Annex records the FCA's compliance with a number of legal requirements applicable to the proposals in this consultation, including an explanation of the FCA's reasons for concluding that our proposals in this consultation are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA).
2. When consulting on new rules, the FCA is required by section 138I(2)(d) FSMA to include an explanation of why it believes making the proposed rules is compatible with (a) its general duty, under s. 1B(1) FSMA, so far as reasonably possible, to act in a way which is compatible with its strategic objective and advances one or more of its operational objectives, and (b) its general duty under s. 1B(5)(a) FSMA to have regard to the regulatory principles in s. 3B FSMA. The FCA is also required by s. 138K(2) FSMA to state its opinion on whether the proposed rules will have a significantly different impact on mutual societies as opposed to other authorised persons.
3. This Annex also sets out the FCA's view of how the proposed rules and guidance are compatible with the duty on the FCA to discharge its general functions (which include rule-making and giving general guidance) in a way which promotes effective competition in the interests of consumers (s. 1B(4)). This duty applies in so far as promoting competition is compatible with advancing the FCA's consumer protection and/or integrity objectives.
4. In addition, this Annex explains how we have considered the recommendations made by the Treasury under s. 1JA FSMA about aspects of the economic policy of Her Majesty's Government to which we should have regard in connection with our general duties.
5. This Annex includes our assessment of the equality and diversity implications of these proposals.
6. Under the Legislative and Regulatory Reform Act 2006 (LRRRA) the FCA is subject to requirements to have regard to a number of high-level 'Principles' in the exercise of some of our regulatory functions and to have regard to a 'Regulators' Code' when determining general policies and principles and giving general guidance (but not when exercising other legislative functions like making rules). This Annex sets out how we have complied with requirements under the LRRRA.

## **The FCA's objectives and regulatory principles: Compatibility statement**

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7. The proposals set out in this consultation are primarily intended to advance the FCA's operational objective of protecting and enhancing the integrity of the UK financial system. They are also relevant to the FCA's consumer protection objective and the competition objective given the impact of more complete and consistent disclosures along the investment chain. Improving the quality and quantity of climate-related disclosures by commercial company issuers of standard listed equity shares, by extending the application of the existing TCFD-aligned disclosure requirements to this wider scope, should further improve the efficiency of asset pricing and capital allocation, reduce consumer harm and increase public confidence in financial markets as set out in more detail in 1.21.
8. We consider these proposals are compatible with the FCA's strategic objective of ensuring that the relevant markets function well as set out in 2.16. For the purposes of the FCA's strategic objective, "relevant markets" are defined by s. 1F FSMA.
9. In preparing the proposals set out in this consultation, the FCA has had regard to the regulatory principles set out in s. 3B FSMA.

### **The need to use our resources in the most efficient and economic way**

10. Referencing the TCFD framework in our proposals allows us to introduce measures in what is a complex and still evolving area of policy in the most efficient manner.

### **The principle that a burden or restriction should be proportionate to the benefits**

11. The Cost Benefit Analysis in Annex 2 sets out the costs and benefits for the proposals set out in this CP. We consider that the benefits of these proposals outweigh the costs.

### **The desirability of sustainable growth in the economy of the United Kingdom in the medium or long term**

12. More complete and consistent disclosures by issuers will support the reallocation of capital throughout the economy to support a smooth transition to a net zero economy.

### **The general principle that consumers should take responsibility for their decisions**

13. Better disclosures by issuers will allow firms to tailor their products to the needs of consumer more effectively. As a result, consumers will benefit from the improved choice of products as well as greater information on their climate-related characteristics.

### **The responsibilities of senior management**

14. We consider that improving the quality and quantity of disclosures is a significant role for senior management. We believe our proposals will enhance the ability of senior management of issuers to take responsibility for their decisions by providing a framework that will encourage them to think about the governance and risk

management of climate-related risks and opportunities, and their companies climate-related strategies. Where issuers are themselves regulated entities, we believe setting out the extended application of our TCFD-aligned requirements will help senior managers to discharge their obligations under the Senior Managers and Certification Regime, where relevant.

### **The desirability of recognising differences in the nature of, and objectives of, businesses carried on by different persons including mutual societies and other kinds of business organisation**

15. We have sought to be proportionate by introducing our rule on a 'comply or explain' basis, in part acknowledging that some firms and sectors may be more or less advanced in their journey to making climate-related disclosures.

### **The desirability of publishing information relating to persons subject to requirements imposed under FSMA, or requiring them to publish information**

16. This principle is not relevant to the proposals set out in this CP.

### **The principle that we should exercise of our functions as transparently as possible**

17. We have sought to be as transparent as possible, indicating our direction of travel for the proposals set out in this CP, both in the Government's Roadmap towards mandatory climate-related disclosures, published in November 2020 as well as PS20/17.
18. In formulating these proposals, the FCA has had regard to the importance of taking action intended to minimise the extent to which it is possible for a business carried on (i) by an authorised person or a recognised investment exchange; or (ii) in contravention of the general prohibition, to be used for a purpose connected with financial crime (as required by s. 1B(5)(b) FSMA).

### **Expected effect on mutual societies**

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19. The FCA does not expect the proposals in this paper to have a significantly different impact on mutual societies as these are typically not listed issuers of equity shares.

### **Compatibility with the duty to promote effective competition in the interests of consumers**

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20. In preparing the proposals as set out in this consultation, we have had regard to the FCA's duty to promote effective competition in the interests of consumers. We consider that the availability of richer data will improve competition. Firms will be enabled to more reliably disclose how their portfolios and products are exposed to climate-related risks and opportunities, helping consumers to assess which products best meet their needs.

## Treasury recommendations about economic policy

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21. We consider that our proposals are consistent with the aspects of the government's economic policy to which the Financial Conduct Authority should have regard.
22. In the remit letter from the Chancellor of the Exchequer to the FCA on 23 March 2021, the Chancellor affirms the FCA's role in protecting consumers, promoting competition in financial services and protecting and enhancing the integrity of the UK financial system.
23. The remit letter provides that the FCA should 'have regard' to the Government's commitment to achieve a net zero economy by 2050 under the Climate Change Act 2008 (Order 2019). We have therefore also considered our work on issuers' climate-related disclosures in this context. We have also had regard to the Treasury's recommendations, as they aim to ensure that financial services markets make a positive contribution to levelling up the country and supporting sustainable economy growth in the UK economy in the medium to long term, while supporting competition between firms operating in this market.
24. Clear disclosure expectations on climate change can help to further underpin the reputation of the London market as a leading venue for high-quality listings, thereby ensuring that the UK remains an attractive domicile for internationally active financial institutions, and that London retains its position as a leading financial centre.

## Equality and diversity

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25. We are required under the Equality Act 2010 in exercising our functions to 'have due regard' to the need to eliminate discrimination, harassment, victimisation and any other conduct prohibited by or under the Act, advance equality of opportunity between persons who share a relevant protected characteristic and those who do not, and to foster good relations between people who share a protected characteristic and those who do not.
26. As part of this, we ensure the equality and diversity implications of any new policy proposals are considered. The outcome of our consideration in relation to these matters in this case is stated in paragraph 2.43-2.45 of this CP.

## Legislative and Regulatory Reform Act 2006 (LRRRA)

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27. We consider that the proposals in this CP have had regard to the 5 LRRRA principles – that regulatory activities should be carried out in a way which is transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed. We have had regard to the Regulators' Code, particularly the requirement for regulatory activity to be proportionate and targeted.

## Annex 4

### Abbreviations in this paper

Abbreviation	Description
<b>AFM</b>	Autoriteit Financiële Markten
<b>AIM</b>	Alternative Investment Market
<b>AMF</b>	Autorité des Marchés Financiers
<b>BEIS</b>	Department for Business, Energy and Industrial Strategy
<b>CBA</b>	Cost benefit analysis
<b>CDSB</b>	Climate Disclosure Standards Board
<b>COP 26</b>	UN Climate Change Summit
<b>CP</b>	Consultation paper
<b>CRA</b>	Credit rating agency
<b>DP</b>	Discussion Paper
<b>DWP</b>	Department for Work and Pensions
<b>EIB</b>	European Investment Bank
<b>ESG</b>	Environmental, Social and Governance
<b>ESMA</b>	European Securities and Market Authority
<b>EU</b>	European Union
<b>FRC</b>	Financial Reporting Council
<b>FS</b>	Feedback Statement
<b>FSB</b>	Financial Stability Board
<b>FSMA</b>	Financial Services and Markets Act 2000
<b>FTE</b>	Full time employee
<b>GDR</b>	Global depositary receipt

Abbreviation	Description
<b>IAASB</b>	International Audit and Assurance Standards Board
<b>ICMA</b>	International Capital Market Association
<b>IFRS</b>	International Financial Reporting Standards
<b>IIRC</b>	International Integrated Reporting Council
<b>IOSCO</b>	International Organisation of Securities Commissions
<b>ISSB</b>	International Sustainability Standards Board
<b>KPI</b>	Key performance indicator
<b>LLP</b>	Limited Liability Partnership
<b>LR</b>	Listing Rule
<b>LSE</b>	London School of Economics
<b>PS</b>	Policy Statement
<b>SASB</b>	Sustainability Accounting Standards Board
<b>SLB</b>	Sustainability-linked bond
<b>SME</b>	Small and medium-sized issuers
<b>SPAC</b>	Special purpose acquisition company
<b>SPO</b>	Second party opinion
<b>SPT</b>	Sustainability performance target
<b>TCFD</b>	Taskforce on Climate-related Financial Disclosures
<b>TN</b>	Technical Note
<b>TWG</b>	Technical Readiness Working Group
<b>UCITS</b>	Undertakings for the Collective Investment in Transferable Securities
<b>UK</b>	United Kingdom
<b>UoP</b>	Use of proceeds
<b>WBCSD</b>	World Business Council for Sustainable Development

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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# Appendix 1

## Draft Handbook text

**LISTING RULES (DISCLOSURE OF CLIMATE-RELATED FINANCIAL  
INFORMATION) (No 2) INSTRUMENT 2021**

**Powers exercised**

- A. The Financial Conduct Authority (“the FCA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 73A (Part 6 Rules);
  - (2) section 96 (Obligations of issuers of listed securities);
  - (3) section 137A (The FCA’s general rules);
  - (4) section 137T (General supplementary powers); and
  - (5) section 139A (Power of the FCA to give guidance).
- B. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on *[date]*.

**Amendments to the Handbook**

- D. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- E. The Listing Rules sourcebook (LR) is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Listing Rules (Disclosure of Climate-Related Financial Information) (No 2) Instrument 2021.

By order of the Board  
*[date]*

## Annex A

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Insert the following new definition in the appropriate alphabetical position. The text is not underlined.

<i>TCFD Technical Supplement on Measuring Portfolio Alignment</i>	the technical supplement entitled [“Technical Supplement on Measuring Portfolio Alignment”] published in [ <i>month</i> ] 2021 by the Task-Force on Climate-related Financial Disclosures, available at: <a href="https://www.fsb-tcfd.org">https://www.fsb-tcfd.org</a> .
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Amend the following definitions as shown.

<i>TCFD Annex</i>	the document entitled “Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures” published in <del>June 2017</del> [ <i>month</i> ] 2021 by the Task Force on Climate-related Financial Disclosures, available at: <a href="https://www.fsb-tcfd.org">https://www.fsb-tcfd.org</a> .
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<i>TCFD Final Report</i>	the report entitled “Recommendations of the Task Force on Climate-related Financial Disclosures” published in <del>June 2017</del> [ <i>month</i> ] 2021 by the Task Force on Climate-related Financial Disclosures, available at: <a href="https://www.fsb-tcfd.org">https://www.fsb-tcfd.org</a> .
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<i>TCFD Technical Supplement on the Use of Scenario Analysis</i>	the technical supplement entitled “The Use of Scenario Analysis in Disclosure of Climate-related Risks and Opportunities” published in June 2017 by the Task Force on Climate-related Financial Disclosures, available at: <a href="https://www.fsb-tcfd.org">https://www.fsb-tcfd.org</a> .
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## Annex B

### Amendments to the Listing Rules sourcebook (LR)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

#### 9 Continuing obligations

...

#### 9.8 Annual financial report

...

9.8.6C G For the purposes of *LR 9.8.6R(8)*, in determining whether a *listed company's* climate-related financial disclosures are consistent with the *TCFD Recommendations and Recommended Disclosures*, the *FCA* considers that the following documents are relevant:

- (1) the *TCFD Final Report* and the *TCFD Annex*, to the extent not already referred to in *LR 9.8.6R(8)* and *LR 9.8.6BG*;
- (2) the *TCFD Technical Supplement on the Use of Scenario Analysis*;
- (3) the *TCFD Guidance on Risk Management Integration and Disclosure*; ~~and~~
- (4) (where appropriate) the *TCFD Guidance on Scenario Analysis for Non-Financial Companies*;
- (5) the [TCFD Guidance on Metrics, Targets and Transition Plans]<sup>1</sup>; and
- (6) (where appropriate) the *TCFD Technical Supplement on Measuring Portfolio Alignment*.

...

#### 14 Standard listing (shares)

...

#### 14.3 Continuing obligations

...

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<sup>1</sup> This is a reference to the proposed standalone TCFD guidance on metrics, targets and transition plans currently being consulted on in the document entitled “Proposed Guidance on Climate-related Metrics, Targets, and Transition Plans”, available at: <https://www.fsb-tcfid.org/publications/>. For further background see paragraph 3.38 of this FCA consultation paper.

Information to be included in annual report and accounts

- 14.3.27    R    In addition to the requirements set out in DTR 4.1, a company with a standard listing of equity shares (other than an investment entity or a shell company) must include a statement in its annual financial report setting out:
- (1) whether the listed company has included in its annual financial report climate-related financial disclosures consistent with the TCFD Recommendations and Recommended Disclosures;
  - (2) in cases where the listed company has:
    - (a) made climate-related financial disclosures consistent with the TCFD Recommendations and Recommended Disclosures, but has included some or all of these disclosures in a document other than the annual financial report:
      - (i) the recommendations and/or recommended disclosures for which it has included disclosures in that other document;
      - (ii) a description of that document and where it can be found; and
      - (iii) the reasons for including the relevant disclosures in that document and not in the annual financial report;
    - (b) not included climate-related financial disclosures consistent with all of the TCFD Recommendations and Recommended Disclosures in either its annual financial report or other document as referred to in (a):
      - (i) the recommendations and/or recommended disclosures for which it has not included such disclosures;
      - (ii) the reasons for not including such disclosures; and
      - (iii) any steps it is taking or plans to take in order to be able to make those disclosures in the future, and the timeframe within which it expects to be able to make those disclosures; and
  - (3) where in its annual financial report or (where appropriate) other document the climate-related financial disclosures referred to in (1) can be found.
- 14.3.28    G    For the purposes of LR 14.3.27R, in determining whether climate-related financial disclosures are consistent with the TCFD Recommendations and Recommended Disclosures, a listed company should undertake a detailed assessment of those disclosures which takes into account:
- (1) Section C of the TCFD Annex entitled “Guidance for All Sectors”;

- (2) (where appropriate) Section D of the *TCFD Annex* entitled “Supplemental Guidance for the Financial Sector”; and
- (3) (where appropriate) Section E of the *TCFD Annex* entitled “Supplemental Guidance for Non-Financial Groups”.

14.3.29    G    For the purposes of LR 14.3.27R, in determining whether a *listed company’s* climate-related financial disclosures are consistent with the *TCFD Recommendations and Recommended Disclosures*, the *FCA* considers that the following documents are relevant:

- (1) the *TCFD Final Report* and the *TCFD Annex*, to the extent not already referred to in LR 14.3.27R and LR 14.3.28G;
- (2) the *TCFD Technical Supplement on the Use of Scenario Analysis*;
- (3) the *TCFD Guidance on Risk Management Integration and Disclosure*;
- (4) (where appropriate) the *TCFD Guidance on Scenario Analysis for Non-Financial Companies*;
- (5) the [TCFD Guidance on Metrics, Targets and Transition Plans]<sup>2</sup>; and
- (6) (where appropriate) the *TCFD Technical Supplement on Measuring Portfolio Alignment*.

14.3.30    G    For the purposes of LR 14.3.27R, in determining whether climate-related financial disclosures are consistent with the *TCFD Recommendations and Recommended Disclosures*, a *listed company* should consider whether those disclosures provide sufficient detail to enable users to assess the *listed company’s* exposure to and approach to addressing climate-related issues.

A *listed company* should carry out its own assessment to ascertain the appropriate level of detail to be included in its climate-related financial disclosures, taking into account factors such as:

- (1) the level of its exposure to climate-related risks and opportunities; and
- (2) the scope and objectives of its climate-related strategy.

noting that these factors may relate to the nature, size and complexity of the *listed company’s* business.

14.3.31    G    (1) For the purposes of LR 14.3.27R, the *FCA* would ordinarily expect a *listed company* to be able to make climate-related financial disclosures consistent with the *TCFD Recommendations and Recommended Disclosures*, except where it faces transitional challenges in obtaining relevant data or embedding relevant modelling or analytical capabilities.

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<sup>2</sup> See footnote 1.

- (2) In particular, the *FCA* would expect that a *listed company* should ordinarily be able to make disclosures consistent with:
- (a) the recommendation and recommended disclosures on governance in the *TCFD Recommendations and Recommended Disclosures*;
  - (b) the recommendation and recommended disclosures on risk management in the *TCFD Recommendations and Recommended Disclosures*; and
  - (c) recommended disclosures (a) and (b) set out under the recommendation on strategy in the *TCFD Recommendations and Recommended Disclosures*, to the extent that the *listed company* does not face the transitional challenges referred to in (1) in relation to such disclosures.

...

Insert the following new definition in the appropriate alphabetical position and amend the existing definitions as shown.

**App 1            Relevant definitions**

**App 1.1        Relevant definitions**

1.1.1            **Note:** The following definitions relevant to the *listing rules* are extracted from the *Glossary*.

...

<i>target</i>	...
<i>TCFD Annex</i>	the document entitled “Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures” published in <del>June 2017</del> <u>[month] 2021</u> by the Task Force on Climate-related Financial Disclosures, available at: <a href="https://www.fsb-tcfd.org">https://www.fsb-tcfd.org</a> .
<i>TCFD Final Report</i>	the report entitled “Recommendations of the Task Force on Climate-related Financial Disclosures” published in <del>June 2017</del> <u>[month] 2021</u> by the Task Force on Climate-related Financial Disclosures, available at: <a href="https://www.fsb-tcfd.org">https://www.fsb-tcfd.org</a> .
...	
<i>TCFD Recommendations and Recommended Disclosures</i>	...

<u>TCFD Technical Supplement on Measuring Portfolio Alignment</u>	the technical supplement entitled [“Technical Supplement on Measuring Portfolio Alignment”] published in [month] 2021 by the Task-Force on Climate-related Financial Disclosures, available at: <a href="https://www.fsb-tcfd.org">https://www.fsb-tcfd.org</a> .
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...	

Insert the following new transitional provision LR TR 16, after LR TR 15 (Transitional Provisions for a prospectus approved before IP completion day). The text is not underlined.

**TR 16 Transitional Provisions in relation to climate-related financial disclosures under LR 14.3.27R**

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1.	LR 14.3.27R	R	LR 14.3.27R applies in relation to a financial year of a <i>listed company</i> beginning on or after 1 January 2022.	From [TBC]	[TBC]



## Appendix 2

### Draft Technical Note

#### Disclosures in relation to ESG matters, including climate change

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Listed issuers, other issuers with securities admitted to trading on regulated markets and other entities in scope of requirements under the Market Abuse Regulation (MAR) and the Prospectus Regulation (PR) are subject to a range of disclosure requirements. The purpose of these requirements is to ensure that shareholders, investors and markets more generally are enabled to make informed decisions.

For example, pursuant to the PR, issuers must consider what disclosures they should make to enable investors to assess (amongst other things) the assets and prospects of the issuer.

A wide range of factors may impact a company's prospects. Climate-related risks and opportunities are widely understood to be financially material to many issuers' assets and therefore may need to be disclosed. Other environmental, social and governance (ESG)-related risks and opportunities are also likely to be financially material to many issuers. Accordingly, issuers should consider ESG matters carefully when determining what should be disclosed under the PR, as well as under the other disclosure regimes.

More broadly, disclosure obligations arise under the Listing Rules and Prospectus Regulation when an issuer's securities are offered to the public, first listed or admitted to trading on a regulated market.

On an ongoing basis, disclosure obligations arise pursuant to the Listing Rules, Disclosure Guidance and Transparency Rules and Market Abuse Regulation:

- in relation to announcements and financial reporting
- on an event-driven basis given that issuers must inform the public as soon as possible of inside information which directly concerns them.

We also note that issuers should assess climate-related risks and opportunities and other ESG considerations carefully in informing their disclosures, both in respect of equity and non-equity securities.

We discuss specific FCA Handbook requirements and obligations set out in EU legislation (which will continue to apply in the UK after the end of the transition period) and how they apply in respect of ESG issues below. The examples of relevant provisions that we provide are not intended to be exhaustive.

## Listing Rules

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Listed issuers need to have appropriate arrangements in place to support their disclosure obligations under various regimes. The Listing and Premium Listing Principles are particularly relevant in this respect.

Listing Principle 1 requires that: *"A listed company must take reasonable steps to establish and maintain adequate procedures, systems and controls to enable it to comply with its obligations."*

Related guidance in LR 7.2.2G further explains that this principle is intended to ensure that listed companies: *"have adequate procedures, systems and controls to enable them to comply with their obligations under the listing rules, disclosure requirements, transparency rules and corporate governance rules. In particular, the FCA considers that listed companies should place particular emphasis on ensuring that they have adequate procedures, systems and controls in relation to, where applicable [...] the timely and accurate disclosure of information to the market."*

In considering whether their procedures, systems and controls are adequate to enable them to comply with their obligations under these various regimes, including the timely and accurate disclosure of information to the market, an issuer should consider whether there is a need to access and draw on specific data sources when disclosing climate-related and other ESG-related risks and opportunities.

An issuer should also consider whether there is a need to develop specific systems, analytical instruments or organisational arrangements to collate and assess the information required to enable it to comply with its obligations.

This recognises that the appropriate consideration of climate-related and other ESG-related matters may require that an issuer accesses data sources that, unlike other indicators of organisational performance, may not typically be used for other business purposes. Furthermore, such data may need to be assessed and analysed using bespoke techniques.

In this respect, LR 7.2.3G further elaborates: *"Timely and accurate disclosure of information to the market is a key obligation of listed companies. For the purposes of Listing Principle 1, a listed company should have adequate systems and controls to be able to:*

- 1.** *ensure that it can properly identify information which requires disclosure under the listing rules, disclosure requirements, transparency rules or corporate governance rules in a timely manner; and*
- 2.** *ensure that any information identified under (1) is properly considered by the directors and that such a consideration encompasses whether the information should be disclosed."*

Additionally, a premium-listed issuer should consider Premium Listing Principle 6. This requires that: *"A listed company must communicate information to holders and potential holders of its premium listed securities and its listed equity shares in such a way as to avoid the creation or continuation of a false market in those premium listed securities and listed equity shares."*

LR 9.8.6R (5) requires that a premium-listed issuer includes within its annual financial report a statement of how the company has applied the Principles set out in the UK Corporate Governance Code 2018, in a manner that would enable shareholders to evaluate how the principles have been applied.

Relatedly, LR 9.8.6R (6) requires the inclusion in its annual financial report of a statement as to whether "*the listed company has (a) complied throughout the accounting period with all relevant provisions set out in the UK Corporate Governance Code; or (b) not complied throughout the accounting period with all relevant provisions set out in the UK Corporate Governance Code and if so, setting out: (i) those provisions, if any it has not complied with; (ii) in the case of provisions whose requirements are of a continuing nature, the period within which, if any, it did not comply with some or all of those provisions; and (iii) the company's reasons for non-compliance.*"

The UK Corporate Governance Code 2018 and its supporting guidance explicitly recognise companies' responsibilities to wider society and provides authoritative guidance on how Boards can ensure strategic importance is given to ESG considerations that are critical to many investors.

LR 9.8.6R(8) and LR 9.8.7R require UK incorporated and overseas commercial companies with a premium listing and LR 14.3.27R requires issuers of standard listed equity shares (excluding standard listed funds and shell companies) to include in their annual financial report "a statement setting out:

- a.** whether the listed company has included in its annual financial report climate-related financial disclosures consistent with the TCFD Recommendations and Recommended Disclosures;
- b.** in cases where the listed company has:
  - i.** made climate-related financial disclosures consistent with the TCFD Recommendations and Recommended Disclosures, but has included some or all of these disclosures in a document other than the annual financial report:
    - A.** the recommendations and/or recommended disclosures for which it has included disclosures in that other document;
    - B.** a description of that document and where it can be found; and
    - C.** the reasons for including the relevant disclosures in that document and not in the annual financial report;
  - ii.** not included climate-related financial disclosures consistent with all of the TCFD Recommendations and Recommended Disclosures in either its annual financial report or other document as referred to in (i):
    - A.** the recommendations and/or recommended disclosures for which it has not included such disclosures;
    - B.** the reasons for not including such disclosures; and
    - C.** any steps it is taking or plans to take in order to be able to make those disclosures in the future, and the timeframe within which it expects to be able to make those disclosures; and
- c.** where in its annual financial report or (where appropriate) other document the climate-related financial disclosures referred to in (a) can be found."

LR 9.8.6BG, LR 9.8.6CG, and LR 9.8.6DG as well as LR 14.3.28G, LR 14.3.29G and LR 14.3.30G provide guidance in relation to determining whether climate-related financial disclosures are consistent with the TCFD Recommendations and Recommended Disclosures.

LR 9.8.6EG and LR 14.3.31G explains that the FCA would ordinarily expect a listed company to be able to "make climate-related financial disclosures consistent with the TCFD Recommendations and Recommended Disclosures, except where it faces transitional challenges in obtaining relevant data or embedding relevant modelling or analytical capabilities."

LR 13.3.1R (1) requires every circular sent by a premium listed company to holders of its listed securities to "*provide a clear and adequate explanation of its subject matter giving due prominence to its essential characteristics, benefits and risks*". In addition, LR 13.3.1R (3) requires every such circular to "*contain all information necessary to allow the security holders to make a properly informed decision*" if voting or other action is required.

In both cases, this may include in relation to ESG matters.

LR 1.3.3R requires that "*An issuer must take reasonable care to ensure that any information it notifies to a RIS or makes available through the FCA is not misleading, false or deceptive and does not omit anything likely to affect the import of the information.*" Again, ESG matters may be relevant here too.

Listing Particulars are discussed in the next section.

## Prospectus Regulation

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### Article 6 of the Prospectus Regulation

When a prospectus is required, it must contain the necessary information which is material to an investor for making an informed assessment of (amongst other things) the assets and prospects of the issuer and of the reasons for the issuance and its impact on the issuer. That information may vary depending on the nature and circumstances of the issuer and the type of securities.

In order to provide adequate information to the market for this purpose, information on climate change and other ESG-related matters may need to be provided where relevant to the issuer. For instance, in the context of the UK Government's target to achieve net-zero carbon emissions by 2050 and to achieve the goals of the Paris Agreement more generally, many companies are likely to need to consider significant changes to their business. Such changes may be material to an investor's assessment of the prospects of the company and the risks and opportunities shaping it.

### Article 14 of the Prospectus Regulation

As a derogation from Article 6, the relevant reduced information to be presented in the simplified prospectus for secondary issuances is that necessary to enable investors to understand the prospects of the issuer and any significant changes in the business and financial position of the issuer since the end of the last financial year. This information

should be written and presented in such a way as to allow investors to make an informed investment decision.

## Risk factors

Recital 54 of the Prospectus Regulation addresses risk factors that are required by the PR and makes specific reference to environmental, social and governance factors. The recital states:

*"The primary purpose of including risk factors in a prospectus is to ensure that investors make an informed assessment of such risks and thus take investment decisions in full knowledge of the facts. Risk factors should therefore be limited to those risks which are material and specific to the issuer and its securities and which are corroborated by the content of the prospectus. A prospectus should not contain risk factors which are generic and only serve as disclaimers, as those could obscure more specific risk factors that investors should be aware of, thereby preventing the prospectus from presenting information in an easily analysable, concise and comprehensible form. Among others, environmental, social and governance circumstances can also constitute specific and material risks for the issuer and its securities and, in that case, should be disclosed. To help investors identify the most material risks, the issuer should adequately describe and present each risk factor in the prospectus. A limited number of risk factors selected by the issuer should be included in the summary."*

Relatedly, in 2019, ESMA published a set of Guidelines on risk factors under the Prospectus Regulation. Guideline 7 on the presentation of risk factors across categories is accompanied by explanatory paragraph 35 which notes that ESG-related risks could form a specific category. Climate change and other ESG factors might also be relevant to other suggested categories of risks, including 'Legal and regulatory'. The ESMA Guidelines provide an example of how ESG risk factors could be disclosed.

## Annexes to the Delegated Prospectus Regulation

Various annexes to the Commission Delegated Prospectus Regulation (EU 2019/980) require relevant disclosures including an overview of the business and a description of the regulatory environment.

Item 5.7.4. Annex 1 requires a description of any environmental issues that may affect the issuer's utilisation of its tangible fixed assets. Item 9.1 requires, on the other hand, a description of the regulatory environment that the issuer operates in and that may materially affect its business, together with information regarding any governmental, economic, fiscal, monetary or political policies or factors that have materially affected, or could materially affect, directly or indirectly, the issuer's operations. Therefore, if the regulatory environment includes environmental matters, they will have to be disclosed, if material.

Item 2.5.1 in Annex 24, requires smaller issuers adopting the new EU Growth prospectus specifically to address environmental matters in covering, to the extent necessary for an understanding of the issuer's business as a whole, an analysis of the development and performance of the issuer's business and its position. The analysis shall include both financial and, where appropriate, non-financial Key Performance Indicators relevant to the particular business, including information relating to environmental and employee matters. This analysis shall, where appropriate, also

include references to, and additional explanations of, amounts reported in the annual financial statements.

Similarly, FSMA requires Listing Particulars to contain all such information as investors and their professional advisers would reasonably require, and reasonably expect to find there, for the purpose of making an informed assessment of the prospects of the issuer of the securities.

ESMA's update of the CESR recommendations, which continue to apply to the extent that they are compatible with the Prospectus Regulation, contains helpful guidance in a number of areas relevant to ESG considerations. This includes guidance on environmental and employee key performance indicators in the context of the operating and financial review (paragraph 28) and identifying factors to consider when preparing profit forecasts (paragraph 50). Specific requirements for mineral companies are set out in paragraphs 131-133 and in Appendices I, II and III. Appendices II and III also contain specific requirements for the Mining and Oil and Gas Competent Persons' Report.

As noted in PMB 31, the European Securities and Markets Authority (ESMA) published its Final Report on new guidelines on prospectus disclosure on 15 July 2020. We will consult on our approach to the guidelines on prospectus disclosure based largely on the new ESMA Guidelines in due course.

LR 4.2 contains further detail on the Listing Particulars and their content, including minimum information requirements.

## Disclosure Guidance and Transparency Rules (DTR)

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Issuers have a number of ongoing disclosures obligations. These disclosures are primarily intended to allow shareholders, investors and the market at large to form a view on the value of traded securities. Implicit in this is that investors need to be put in a position to be able to assess the prospects of the company and the risks and opportunities shaping it.

In order to provide adequate information to the market for this purpose, information on climate change and other ESG-related matters may need to be provided where relevant to the issuer. For instance, in the context of the UK Government's target to achieve net-zero carbon emissions by 2050 and to achieve the goals of the Paris Agreement more generally, many companies are likely to need to consider significant changes to their business. Such changes may be material to an investor's assessment of the prospects of the company and the risks and opportunities shaping it.

The Disclosure Guidance and Transparency Rules (DTR) require that the Management Report in the Annual Financial Report and the Interim Management Report in the Half-Yearly Financial Report contain a description of the principal risks and uncertainties facing the issuer (DTR 4.1.8R and DTR 4.2.7R, respectively).

The Management Report in the Annual Financial Report must also contain a fair review of the issuer's business. DTR 4.1.9R requires the inclusion in that review, to the extent necessary for an understanding of the development, performance or position of the issuer's business, of analysis using key performance indicators. This should

include information relating to environmental matters and employee matters where appropriate.

DTR 7.2 requires an issuer to include a corporate governance statement in its directors' report, or in a separate report published with its annual report or made available on its website. DTR 7.2 includes information requirements in relation to any relevant corporate governance code (DTR 7.2.2R and DTR 7.2.3R), the issuer's internal control and risk management systems in relation to the financial reporting process (DTR 7.2.5R), and the diversity policy applied to the issuer's administrative, management and supervisory bodies (DTR 7.2.8AR).

DTR 1A.3.2R requires an issuer to "*take all reasonable care to ensure that any information it notifies to a RIS is not misleading, false or deceptive and does not omit anything likely to affect the import of the information.*" This may include in relation to ESG matters.

## Market Abuse Regulation (MAR)

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Pursuant to Article 17 of MAR, an issuer must publicly disclose inside information that directly concerns them as soon as possible, unless the conditions for delay are met. This includes any inside information that relates to climate change and other ESG-related matters.

Article 17(1) clarifies that "*The issuer shall ensure that the inside information is made public in a manner which enables fast access and complete, correct and timely assessment of the information by the public...*"

When disclosing climate-related and other ESG-related information, an issuer must not do so in a way (for example by omitting information) that breaches the prohibition of market manipulation under Article 15 of MAR, noting the relevant behaviours defined in Article 12 of MAR that amount to market manipulation. These include, but are not limited to, dissemination of information which is likely to give false or misleading signals as to the supply of, demand for, or price of a financial instrument.

In this regard, recital 47 adds: "*The manipulation or attempted manipulation of financial instruments [...] may consist in the invention of manifestly false information, but also the wilful omission of material facts, as well as the knowingly inaccurate reporting of information.*"

## Appendix 3

# The TCFD's recommendations and recommended disclosures

This Appendix sets out the TCFD recommendations, supporting recommended disclosures as well as guidance for all sectors and supplemental guidance for the financial sector and non-financial groups in Figures A to G.

### Figure A – the TCFD Recommendations and Recommended Disclosures

Governance	Strategy	Risk Management	Metrics and Targets
Disclose the organization's governance around climate-related risks and opportunities.	Disclose the actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning where such information is material.	Disclose how the organization identifies, assesses, and manages climate-related risks.	Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.
Recommended Disclosures	Recommended Disclosures	Recommended Disclosures	Recommended Disclosures
a) Describe the board's oversight of climate-related risks and opportunities.	a) Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term.	a) Describe the organization's processes for identifying and assessing climate-related risks.	a) Disclose the metrics used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process.
b) Describe management's role in assessing and managing climate-related risks and opportunities.	b) Describe the impact of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning.	b) Describe the organization's processes for managing climate-related risks.	b) Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.
	c) Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.	c) Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organization's overall risk management.	c) Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets.

Source: Final Report, Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017



## Figure B – Governance: Guidance for all sectors

Governance	
Disclose the organization's governance around climate-related risks and opportunities.	
<b>Recommended Disclosure a)</b> Describe the board's oversight of climate-related risks and opportunities.	<b>Guidance for All Sectors</b> In describing the board's oversight of climate-related issues, organizations should consider including a discussion of the following: <ul style="list-style-type: none"> <li>– processes and frequency by which the board and/or board committees (e.g., audit, risk, or other committees) are informed about climate-related issues,</li> <li>– whether the board and/or board committees consider climate-related issues when reviewing and guiding strategy, major plans of action, risk management policies, annual budgets, and business plans as well as setting the organization's performance objectives, monitoring implementation and performance, and overseeing major capital expenditures, acquisitions, and divestitures, and</li> <li>– how the board monitors and oversees progress against goals and targets for addressing climate-related issues.</li> </ul>
<b>Recommended Disclosure b)</b> Describe management's role in assessing and managing climate-related risks and opportunities.	<b>Guidance for All Sectors</b> In describing management's role related to the assessment and management of climate-related issues, organizations should consider including the following information: <ul style="list-style-type: none"> <li>– whether the organization has assigned climate-related responsibilities to management-level positions or committees; and, if so, whether such management positions or committees report to the board or a committee of the board and whether those responsibilities include assessing and/or managing climate-related issues,</li> <li>– a description of the associated organizational structure(s),</li> <li>– processes by which management is informed about climate-related issues, and</li> <li>– how management (through specific positions and/or management committees) monitors climate-related issues.</li> </ul>

Source: Final Report, Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017

## Figure C – Strategy: Guidance for all sectors

Strategy	
Disclose the actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning where such information is material.	
<b>Recommended Disclosure a)</b> Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term.	<b>Guidance for All Sectors</b> Organizations should provide the following information: <ul style="list-style-type: none"> <li>– a description of what they consider to be the relevant short-, medium-, and long-term time horizons, taking into consideration the useful life of the organization's assets or infrastructure and the fact that climate-related issues often manifest themselves over the medium and longer terms,</li> <li>– a description of the specific climate-related issues for each time horizon (short, medium, and long term) that could have a material financial impact on the organization, and</li> <li>– a description of the process(es) used to determine which risks and opportunities could have a material financial impact on the organization.</li> </ul> Organizations should consider providing a description of their risks and opportunities by sector and/or geography, as appropriate. In describing climate-related issues, organizations should refer to <a href="#">Tables 1</a> and <a href="#">2</a> (pp. 10-11).
<b>Recommended Disclosure b)</b> Describe the impact of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning.	<b>Guidance for All Sectors</b> Building on recommended disclosure (a), organizations should discuss how identified climate-related issues have affected their businesses, strategy, and financial planning. Organizations should consider including the impact on their businesses and strategy in the following areas: <ul style="list-style-type: none"> <li>– Products and services</li> <li>– Supply chain and/or value chain</li> <li>– Adaptation and mitigation activities</li> <li>– Investment in research and development</li> <li>– Operations (including types of operations and location of facilities)</li> </ul> Organizations should describe how climate-related issues serve as an input to their financial planning process, the time period(s) used, and how these risks and opportunities are prioritized. Organizations' disclosures should reflect a holistic picture of the interdependencies among the factors that affect their ability to create value over time. Organizations should also consider including in their disclosures the impact on financial planning in the following areas: <ul style="list-style-type: none"> <li>– Operating costs and revenues</li> <li>– Capital expenditures and capital allocation</li> <li>– Acquisitions or divestments</li> <li>– Access to capital</li> </ul> If climate-related scenarios were used to inform the organization's strategy and financial planning, such scenarios should be described.

<p><b>Recommended Disclosure c)</b> Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.</p>	<p><b>Guidance for All Sectors</b> Organizations should describe how resilient their strategies are to climate-related risks and opportunities, taking into consideration a transition to a lower-carbon economy consistent with a 2°C or lower scenario and, where relevant to the organization, scenarios consistent with increased physical climate-related risks.</p> <p>Organizations should consider discussing:</p> <ul style="list-style-type: none"> <li>– where they believe their strategies may be affected by climate-related risks and opportunities;</li> <li>– how their strategies might change to address such potential risks and opportunities; and</li> <li>– the climate-related scenarios and associated time horizon(s) considered.</li> </ul> <p>Refer to <a href="#">Section D</a> for information on applying scenarios to forward-looking analysis.</p>
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Source: Final Report, Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017

## Figure D – Risk Management: Guidance for all sectors

<p><b>Risk Management</b> Disclose how the organization identifies, assesses, and manages climate-related risks.</p>	
<p><b>Recommended Disclosure a)</b> Describe the organization's processes for identifying and assessing climate-related risks.</p>	<p><b>Guidance for All Sectors</b> Organizations should describe their risk management processes for identifying and assessing climate-related risks. An important aspect of this description is how organizations determine the relative significance of climate-related risks in relation to other risks.</p> <p>Organizations should describe whether they consider existing and emerging regulatory requirements related to climate change (e.g., limits on emissions) as well as other relevant factors considered.</p> <p>Organizations should also consider disclosing the following:</p> <ul style="list-style-type: none"> <li>– processes for assessing the potential size and scope of identified climate-related risks and</li> <li>– definitions of risk terminology used or references to existing risk classification frameworks used.</li> </ul>
<p><b>Recommended Disclosure b)</b> Describe the organization's processes for managing climate-related risks.</p>	<p><b>Guidance for All Sectors</b> Organizations should describe their processes for managing climate-related risks, including how they make decisions to mitigate, transfer, accept, or control those risks. In addition, organizations should describe their processes for prioritizing climate-related risks, including how materiality determinations are made within their organizations.</p> <p>In describing their processes for managing climate-related risks, organizations should address the risks included in <a href="#">Tables 1</a> and <a href="#">2</a> (pp. 10-11), as appropriate.</p>

<b>Recommended Disclosure c)</b> Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organization's overall risk management.	<b>Guidance for All Sectors</b> Organizations should describe how their processes for identifying, assessing, and managing climate-related risks are integrated into their overall risk management.
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Source: Final Report, Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017

## Figure E – Metrics and Targets: Guidance for all sectors

Metrics and Targets Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.	
<b>Recommended Disclosure a)</b> Disclose the metrics used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process.	<b>Guidance for All Sectors</b> Organizations should provide the key metrics used to measure and manage climate-related risks and opportunities, as described in <a href="#">Tables 1 and 2</a> (pp. 10-11). Organizations should consider including metrics on climate-related risks associated with water, energy, land use, and waste management where relevant and applicable.  Where climate-related issues are material, organizations should consider describing whether and how related performance metrics are incorporated into remuneration policies.  Where relevant, organizations should provide their internal carbon prices as well as climate-related opportunity metrics such as revenue from products and services designed for a lower-carbon economy.  Metrics should be provided for historical periods to allow for trend analysis. In addition, where not apparent, organizations should provide a description of the methodologies used to calculate or estimate climate-related metrics.
<b>Recommended Disclosure b)</b> Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.	<b>Guidance for All Sectors</b> Organizations should provide their Scope 1 and Scope 2 GHG emissions and, if appropriate, Scope 3 GHG emissions and the related risks. <sup>39</sup>  GHG emissions should be calculated in line with the GHG Protocol methodology to allow for aggregation and comparability across organizations and jurisdictions. <sup>40</sup> As appropriate, organizations should consider providing related, generally accepted industry-specific GHG efficiency ratios. <sup>41</sup>  GHG emissions and associated metrics should be provided for historical periods to allow for trend analysis. In addition, where not apparent, organizations should provide a description of the methodologies used to calculate or estimate the metrics.

<b>Recommended Disclosure c)</b>	<b>Guidance for All Sectors</b>
Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets.	<p>Organizations should describe their key climate-related targets such as those related to GHG emissions, water usage, energy usage, etc., in line with anticipated regulatory requirements or market constraints or other goals. Other goals may include efficiency or financial goals, financial loss tolerances, avoided GHG emissions through the entire product life cycle, or net revenue goals for products and services designed for a lower-carbon economy.</p> <p>In describing their targets, organizations should consider including the following:</p> <ul style="list-style-type: none"> <li>– whether the target is absolute or intensity based,</li> <li>– time frames over which the target applies,</li> <li>– base year from which progress is measured, and</li> <li>– key performance indicators used to assess progress against targets.</li> </ul> <p>Where not apparent, organizations should provide a description of the methodologies used to calculate targets and measures.</p>

Source: Final Report, Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017

## Figure F: Supplemental Guidance for the Financial Sector and Non-Financial Groups

		Governance		Strategy			Risk Management			Metrics and Targets		
Industries and Groups		a)	b)	a)	b)	c)	a)	b)	c)	a)	b)	c)
Financial	Banks			■			■			■		
	Insurance Companies				■	■	■	■		■		
	Asset Owners				■	■	■	■		■	■	
	Asset Managers				■		■	■		■	■	
Non-Financial	Energy				■	■				■		
	Transportation				■	■				■		
	Materials and Buildings				■	■				■		
	Agriculture, Food, and Forest Products				■	■				■		

Source: Final Report, Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017

**Figure G: Location of Supplemental Guidance for the Financial Sector and Non-Financial Groups in the document entitled “Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures”**

		Governance		Strategy			Risk Management			Metrics and Targets		
	Industries and Groups	a)	b)	a)	b)	c)	a)	b)	c)	a)	b)	c)
Financial	Banks			p24			p25			p26		
	Insurance Companies				p29	p30	p30	p31		p31		
	Asset Owners				p35	p35	p35	p36		p36	p37	
	Asset Managers				p39		p40	p 40		p41	p42	
Non-Financial					p48	p48				p50		

