GLOBAL RISK INSTITUTE

To: The Secretary of the Ontario Securities Commission
Email: comment@osc.gov.on.ca
Re: Request for Comment on Proposed National Instrument 51-107 Climate-related Matters
From: Submission by the Global Risk Institute in Financial Services

Contact: Sonia Baxendale, President and CEO [redacted], and Alyson Slater, Senior Director, Sustainable Finance [redacted]

Date: December 20, 2021

Dear Secretary,

Thank you for the opportunity to comment on the proposed National Instrument 51-107 and its companion policy regarding the disclosure of climate-related financial matters.

The Global Risk Institute in Financial Services (GRI) is a member services organization founded by the public and private sectors in Canada. Our members include Canadian pension funds, banks, insurers, financial Crown corporations, and Provincial and Federal governing bodies. We are the premier thought leadership organization in risk management for the financial industry, and bring together leaders from industry, academia, and government to draw actionable insights on risk management, including climate risk. We have significant climate risk management and reporting expertise.

We are submitting our comments on the proposed National Instrument 51-107 drawing on our climate risk management and reporting expertise and knowledge of best practice in Canada and globally. We welcome the instrument's alignment with the Task Force for Climate Related Financial Disclosures (TCFD) Recommendations in light of its global acceptance by major governments, investors and issuers; its adoption by the IFRS' International Sustainability Standards Board (ISSB) as a starting point for a global standard; and the Canadian federal governments' stated intention to move toward mandatory TCFD reporting with the inputs of the Sustainable Finance Action Council (SFAC).

We support CSA's stated goals of: improving issuer access to global capital markets by aligning Canadian disclosure standards with expectations of international investors; assisting investors in making more informed investment decisions by enhancing climate-related disclosures; facilitating comparable and consistent disclosure; and reducing costs, inefficiency and market fragmentation associated with reporting to multiple disclosure frameworks. It is with these principles in mind that we present the following commentary on the proposed National Instrument 51-107.

Investors and lenders in Canada and globally have made net zero portfolio carbon emissions commitments aligned with Canada's national targets and require, with some urgency, climate related financial information from issuers and counterparties in order to ensure capital is aligned with these targets. It is in the best interests of Canadian issuers that they are able to keep up with global reporting expectations on climate, which are largely based on the TCFD Recommendations today, and are sure to become more rigorous as global standards are produced by the ISSB.

Following are our views on the modifications that CSA has proposed in the National Instrument 51-107 versus the original TCFD Recommendations.

Commentary on areas of divergence between 51-107 and the TCFD Recommendations

Scenario Analysis

Climate risk scenario analysis is a key tool in helping firms of all sizes understand what the future may hold in terms of physical and transition risk, can inform materiality assessment and business strategy and should therefore be included as a reporting requirement in the National Instrument. With full recognition that climate scenario analysis is still in its early stages, is not yet standardized, and is hindered by availability of credible data, it is still important that firms get started with building capacity to conduct scenario analysis as this field evolves, and communicate to investors that they are aware of major climate-related risks and how they are likely to impact their business.

Bank of Canada and OSFI are underway with a climate-change scenario pilot project involving six financial sector issuers that will inform more specific scenario and risk management requirements in Canada going forward. Major economies such as the UK, US, Europe and others are also underway with formal scenario analysis programs in an effort to build capacity in companies and accelerate this practice. Mandatory scenario analysis is the direction of travel in most major markets.

The National Instrument 51-107 could vary requirements for reporting on climate scenario analysis for firms as a reflection of the material risk they face. For example, higher standards should apply to larger firms due to their importance for financial sector or general market stability. Whereas smaller firms that face material financial risk from climate change could be given the flexibility to utilize qualitative or narrative-based scenarios aimed at improving their understanding of key issues such as changing carbon prices or potential physical risk exposures under different temperature scenarios. Expectations could become more rigours over time as capacity builds.

Scope 1, 2 and 3 emissions

Currently, the TCFD Recommendations state that firms should report scope 1 and scope 2 emissions regardless of materiality, and Scope 3 should be reported if deemed material, which it is deemed to be for firms in moderate to high emissions sectors.

All firms should be expected to disclose Scope 1 and Scope 2 GHG emissions, using the GHG Protocol. This data is generally available and accessible to Canadian issuers through existing environmental compliance reporting and via the utility companies that supply energy to issuers. Scope 2 emissions can often be easier for smaller issuers to report even than Scope 1 emissions due to the regulated nature of Canada's utility sector and the availability of detailed information on energy purchased and used by clients.

It is recognized that Scope 3 emissions are more difficult to measure because they relate to carbon emissions in the issuer's value chain from entities not directly controlled by the issuer, and for complexities relating to double counting. Yet Scope 3 emissions are often a much larger source of emissions for issuers than Scope 1 and 2 combined, and are often the greatest source of transition risk. As a result, Scope 3 emissions are of interest to investors. In the absence of self-reported Scope 3 emissions, analysts will commonly estimate or model these emissions for firms and will assume a larger carbon footprint to ensure a conservative estimate in light of data uncertainties - which is a practice that does not favour the issuer.

The process of assessing and disclosing Scope 3 emissions will help all issuers better understand the size and nature of their carbon exposure, and is the foundational building block of any low carbon transition plan.

Of the 30 major Canadian financial institutions reporting aligned with TCFD, nearly 80 per cent of them already disclose Scope 3 emissions, and CSA's own research showed that 50 per cent of Canadian issuers have disclosed Scope 3 emissions. There is an opportunity to harness this momentum by enforcing Scope 3 emissions reporting for large issuers, giving smaller firms a timeframe within which to estimate or calculate their Scope 3 emissions. The GHG Protocol and the Partnership for Carbon Accounting Financials (PCAF) give adequate guidance for calculating Scope 3 emissions for most firms.

GHG Protocol

The Greenhouse Gas Protocol (GHG Protocol) is the long-accepted global standard for GHG emissions calculations and underpins the emissions reporting indicators in all of the widely used global voluntary reporting standards (including GRI Standards, SASB, CDP, TCFD, and others), and is integrated into the climate risk reporting prototype issued by the ISSB. Uptake of the GHG Protocol by Canadian firms is widespread, as it is among the world's largest and publicly traded firms. In support of the CSA's intention to improve comparability and consistency, reduce cost and fragmentation, reporting in alignment with the GHG Protocol should be a requirement for all new reporting entities, and a timeframe for existing issuers not yet aligned with the GHG Protocol to make the transition should be incorporated into the National Instrument.

Materiality Assessment

Materiality assessment is a foundational element of all risk management, including climate risk, and a key component of strategy development. Investors seek to understand if a materiality assessment has been conducted, and what the material risks are for all firms, regardless of size. Techniques or tools adopted by issuers to assess the materiality of climate change to their business include using a risk log, scenario analysis, alignment with voluntary sector standards such as SASB, peer comparison, stakeholder engagement, and others. For those issuers who define certain climate-related risks as immaterial, a detailed explanation should be provided backed by concrete data and evidence to avoid omitting any climate-related information that is material for investors.

Assurance on GHG Emissions Reporting

Requiring assurance on reported GHG emissions data could lead to extra costs for the issuer, yet the process helps build rigour in internal processes and systems and improves confidence for investors in the quality of the data. As investors grow to expect more granular disclosure of climate-related risks and opportunities in annual reports it can be expected that assurance will support the accuracy, reliability, comparability, and timeliness of such data.

Reporting by Smaller and Venture Firms

In general, smaller firms will need more time to reach the level of disclosure that some larger issuers have already achieved voluntarily, yet arguably face greater risks due to characteristics such as smaller capital buffers, less diversification, and less developed climate risk governance and management.

Our strong advice is that reporting requirements for smaller firms be linked to the material risk they face from climate change rather than base the reporting requirements on their size or other measures. Canada's issuers are largely from high emissions, high climate risk sectors and although many may lack the resources and capacity to manage and report climate risk today, it will be essential for their competitiveness and survival that they develop these capabilities.

Reporting requirements can be phased in, over a longer period of time, for venture firms – but a clear path should be presented in order to incentivize these issuers to get started with foundational steps in climate risk management and assessment. We must consider the broader global context in which these issuers exist. Although they operate here in Canada, they have global investors and are a part of global value chains. Reporting in alignment with global expectations will help smaller issuers remain ahead of the pack on climate risk.

The concept of safe harbour should be applied to all issuers that are early on their climate risk and reporting journey. There is no historic precedent for this sort of reporting, and all parties (regulators, issuers, investors, data users of all sorts) have much to learn about the practice. If the firm is making a good-faith effort they should have protection for a reasonable period to encourage better quality and quantity of reporting.

Outlook

In light of the Glasgow Climate Pact where most economies committed to net zero emissions by 2050 and aggressive emissions cuts by 2030, and the widespread adoption of the Glasgow Financial Alliance for Net Zero by hundreds of financial institutions globally, Canadian firms need to stay ahead of climate risk to remain competitive in the changing policy and investor landscape. National Instrument 51-107 is one mechanism through which issuers large and small can provide data to investors about their climate risks and opportunities, and will stimulate the important internal work of developing climate governance and leadership, strategy, risk management and targets. We look forward to a National Instrument that is fully aligned with the widely adopted guidance available to-date in the form of the TCFD Recommendations, which will benefit Canadian issuers in anticipation of more rigorous international standards on the near-term horizon.