ICMA
International Capital Market Association

COMMENTS
FCA Consultation on Climate change and Green Finance

General comments

- ICMA agrees with the FCA's assessment that climate change is an important topic that is likely to have a significant impact on financial services markets. We also concur with the view expressed by the Central Banks and Supervisors Network for Greening the Financial System (NGFS) that climate change may pose a risk to financial stability as outlined in its October 2018 report: "Climate change will affect the global economy and so the financial system that supports it. The financial risks it presents are in consequence system-wide and potentially irreversible if not addressed"
- The transition to a sustainable global economy requires a scaling up of the financing of investments that provide environmental and social benefits. The bond markets through Green, Social and Sustainability Bonds can play an essential role in attracting private capital to finance these global needs. In this context, ICMA serves as Secretariat to the Green Bond Principles, Social Bond Principles and the Sustainability Bond Guidelines, which have become the leading frameworks globally for issuance of green, social and sustainability bonds. Further information is available on the ICMA website.

Questions embedded in the Discussion Paper DP18/8

Q1 (5.16): What, if any, difficulties do issuers face in determining materiality? We are also interested in exploring how investors consider materiality in this context?

- Issuers will consider climate related risks to be material when they have the potential to impact the operational continuity of an issuer's activities and the financial strength of its organisation.
- The information that is material to investors in debt securities is that which relates to the ability of the issuer to meet its obligations under the debt security, as reflected in the disclosure requirements of the EU Prospectus Directive and forthcoming EU Prospectus Regulation[1]. Investors undertake credit analysis and look to indicators such as credit ratings when they assess an issuer's ability to meet its obligations, but not all relevant information to capture and reflect risks arising from climate change is currently available.
- Non-financial disclosure of relevant risks related to the impact of climate change will help investors to determine materiality by improving the understanding of investors of the scope of issuers' exposure to climate risk and its potential to impact business operations and creditworthiness.

[1] See, for example, EU Delegated Regulation 809/2004, as amended, Annex IV, item 4.

Q2 (5.17): We are interested in understanding whether greater comparability of disclosures would help investors in their decision-making more generally. If so, what framework could be most useful?

- Comparability and consistency are key for non-financial disclosure to provide useful information for investors in their assessment and decision-making. This disclosure should be part of the regular annual and semi-annual reporting regime, so that it is generally available to market users. The recommendations of the TCFD (Task Force for Climate-related Financial Disclosure) provide a framework designed to help issuers structure their reporting. The TCFD framework is increasingly recognized by market participants, both in the corporate world and in the financial industry, and in some jurisdictions, it is being adopted into regulation.

Q3 (5.22): Would exploring a 'comply or explain' approach, or other avenues to encourage more consistent disclosure, be an effective way of facilitating more effective markets?

- A voluntary 'comply or explain' approach would motivate issuers to consider and assess climate-related risks for their business operations. It will inform investors that the issuer is cognisant of climate-related risks and has assessed how climate risks may impact its business.

Q1 (5.25): Do you think that a requirement for firms to report on climate risk would be a valuable measure?

- A voluntary 'comply or explain' approach would be preferable as a mandatory requirement may pre-empt the further development of flexible market-based initiatives and recommendations as exemplified by the TCFD. Best practice on reporting is also likely to emerge from the increasing expectations of the investor community where sustainability considerations are rapidly mainstreaming.

Q2 (5.26): Do you have any suggestions for what information could be included in a climate risks report?

- The TCFD framework focuses on four key areas (strategy, governance, risk management and metrics & targets) that reflect the types of information investors and other market participants expressed that they need to make better, more informed decisions. It establishes the basis for a consistent, comparable, reliable, clear, and efficient reporting framework. It should be noted, however, that this approach is appropriate in the context of an annual or semi-annual reporting regime (for example, under the Transparency Directive).

Q3 (5.27): Do you have any views on which regulated firms should be required to compile a climate risk report?

- We believe that all regulated firms should be encouraged to provide voluntary disclosures based on their assessment of the materiality of their exposure to climate related risks and the guidance and methodologies provided by the TCFD.

Additional Questions (Section 8)

1. **How can authorities, including the FCA, most effectively work with industry to meet investor demand for green investment opportunities and encourage those raising capital and investing in it to pursue sustainable outcomes?**

- The FCA should maintain an open dialogue with the green investment segment of the market such as the Green Bond Principles supported by ICMA and reach out to other relevant financial industry associations. It will also be useful to collaborate with the green and responsible investor community as represented for example by as the PRI (Principles for Responsible Investment).
- The FCA should review incentive structures for green finance used in other jurisdictions and consider whether any of these would be recommendable in the UK.
- The FCA should also support disclosure efforts such as TCFD and ensure compatibility with ongoing European Union initiatives in this area.

2. **Do you agree with the extent of the FCA's proposed interventions on climate change-related financial disclosures? Is there a specific need for us to intervene further in the interests of market integrity or consumer interests?**

- We agree with the extent of the FCA's approach subject to our comments included in this response.

3. **In light of the EU work on taxonomy, what are your views on the form, common standards and metrics for measuring and reporting against green financial services products should take?**

- The EU's work on a taxonomy is a very significant development. We will be responding to the current consultation on its usability. We would recommend that the FCA follow closely the debate around the taxonomy and draw its own conclusions on market impact. The FCA should also aim to ensure the compatibility of any comparable initiatives that may be considered in the UK context post Brexit.

4. **How could regulators and industry best work together as part of the Climate Financial Risk Forum?**

- An increasing awareness among investors of the potential implications of climate change on the value of their portfolio is causing responsible investors to integrate environmental, social and governance issues into their investment processes.
- ICMA remains at the disposal of the FCA to engage with the Climate Financial Risk Forum.
- The FCA should also reach out to other relevant financial industry associations.

5. **What are your biggest concerns and commercial priorities regarding climate change?**

- The potential impact of inaction on future financial stability. As stated by Mark Carney, Governor of Bank of England and Chairman of the Financial Stability Board, "Climate change is a tragedy of the horizon which imposes a cost on future generations that the current one has no direct incentive to fix."
- Changes in policy, technology and physical risks related to climate change could prompt a reassessment of the value of a large range of assets as costs and opportunities become apparent. The speed at which such re-pricing occurs is uncertain and could be material for financial stability. Regulators should consider these emerging vulnerabilities with the support of appropriate disclosures and transparency of information.

6. **What are the biggest barriers to the growth of green financial services in the UK?**

- While there is growing political and market support for green finance, all market participants may not yet be convinced of its value due to, among other things, a lack of awareness of the potential risks that climate change and environmental issues create for financial stability and the economy overall, a short-term view and confusion of what qualifies as green (enough).
- However, as the cost of inaction increases with the crystallisation of climate related liabilities and risks, green financial services will likely rapidly become an increasingly attractive option in support of corporate climate change mitigation and transition strategies.