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Canada Releases New Climate-Focused Guideline for Banks and Insurers

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On March 7, 2023, the Office of the Superintendent of Financial Institutions ("OSFI"), the Canadian government agency responsible for supervising federally-regulated financial institutions ("FRFI") and insurance companies, released a new **guideline** ("Guideline") on climate risk management. The Guideline will become effective in fiscal year 2024 for "Domestic Systemically Important Banks" and "Internationally Active Insurance Groups headquartered in Canada" and in fiscal year 2025 for smaller financial institutions. OSFI released the Guideline following a public consultation that generated over 4,300 submissions, which the accompanying press release **reported** is "one of the most extensive consultations in OSFI's history."

The Guideline identifies three broad goals for FRFIs: 1) understand and mitigate potential impacts of climate-related risks to its business model and strategy; 2) implement appropriate governance and risk management practices to manage identified climate-related risks; and 3) remain financially resilient through "severe, yet plausible, climate risk scenarios, and operationally resilient through disruption due to climate-related disasters."

The guidance document itself comprises two chapters. The first covers governance and risk management principles, expectations, and best practices. The governance section requires FRFIs to develop and implement a Climate Transition Plan for managing climate-related risk in line with each entity's business plan and strategy, including assessments of achievability under different climate-related scenarios, as well as internal progress and success metrics. The guidance notes that "senior Management has overall accountability for the FRFI's climate risk management," and suggests (but does not require) that compensation policies should be tied to climate-related risk considerations.

The risk management section makes clear that FRFIs must develop robust systems and processes for identifying, managing, monitoring, and reporting on climate-related risks, including through the use of climate scenario analyses to stress test their risk profiles, business models, strategies, and the adequacy of capital and liquidity buffers. OSFI also plans to require FRFIs to complete standardized climate scenario exercises, in addition to undertaking bespoke climate scenario analyses, and to report the results of OSFI-devised analyses to the regulator periodically.

The second chapter of the Guideline outlines a detailed set of expectations for the substance, format, and timing of required climate-related financial disclosures, which are to be aligned with the recommendations of the Task Force on Climate-related Financial Disclosures ("TCFD"). The disclosure expectations are premised on the principles of relevance, specificity and comprehensiveness, clarity, quality and reliability, appropriateness, and consistency. Reporting is required at least annually. FRFIs must make their climate-related disclosures publicly available "no later than 180 days after fiscal year-end," and must maintain "an ongoing archive of all disclosures relating to prior reporting periods."

The minimum mandatory financial disclosure template annexed to the Guideline includes, among other things, disclosure of:

- metrics and targets used by the financial institution to assess climate-related risks and opportunities;
- Scope 1, 2, and 3 greenhouse gas emissions; and
- any public climate-related commitment(s) whether through an industry-led Net-Zero alliance or otherwise.

According to the Superintendent, the Guideline "balances the concerns of stakeholders in all regions of Canada and remains in line with the expectations of global and domestic investors who fund Canadian federally regulated financial institutions."

Taking the Temperature: Canada is the latest jurisdiction to introduce updated climate-related reporting requirements and risk management expectations for financial institutions and insurance companies, with similar initiatives advanced in other jurisdictions, including the EU, Switzerland, and the UK. Similar to these regulatory efforts, Canada's Guidance focuses on governance, disclosure, and overall financial resilience. As we have reported, financial institutions appear to be moving ahead proactively with enhanced climate-related disclosure and governance mechanisms, with evidence coming from recent reports from Citi and Deutsche Bank and HSBC. For example, Citi recently stated that it "expanded [its] Board of Directors' oversight of certain climate-related matters such as climate risk and climate and ESG disclosures;" "[c]odified the integration of climate-related issues with certain Board committees, including incorporating oversight of our climate disclosure risk and controls environment into the Audit Committee (AC) charter and climate risk oversight into the Risk Management Committee (RMC) charter;" "[c]ommenced an ESG Disclosure Committee to support the Board and AC and provide oversight of Citi's disclosure controls and procedures;" and "[e]xpanded and realigned our Climate Risk team to be part of the Enterprise Risk Management function within Risk and further added subject

matter expertise." Citi added that it also continues to "educate [its] entire Board, as well as senior management, to build out climate-related expertise and capabilities," and that "sustainability and climate-related goals are incorporated into several executive scorecards, which are key elements of performance management tied to the determination of incentive compensation for these executives." While the U.S. climate-related regulatory scheme lags Europe, the Federal Reserve, the SEC, and other financial services and securities market regulators have issued proposed rules or high-level guidance akin to what has been issued elsewhere and, notwithstanding the somewhat unique "anti-ESG" movement in the U.S., we expect the U.S. regulatory framework to continue to evolve over time.