Clients&FriendsMemo

UK's Financial Conduct Authority Consults on New Climate-Related Disclosure Requirements following TCFD Recommendations

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Introduction

In March 2020, the UK's Financial Conduct Authority (the "**FCA**") released a consultation paper entitled: "*Proposals to enhance climate-related disclosures by listed issuers and clarification of existing disclosure obligations*" ("**CP20/3**").

The proposal would introduce a new listing requirement for commercial companies with a Premium Listing on the London Stock Exchange. If implemented, these companies' annual reports for financial years beginning on or after 1 January 2021, will have to include climate-related disclosure as recommended by the Taskforce on Climate-related Financial Disclosures ("**TCFD**"), and/or to explain any non-compliance. The deadline for comments and feedback on CP20/3 is 5 June 2020. Following consideration of the feedback received on CP20/3, the FCA aims to publish a Policy Statement, along with the finalised rules and an FCA Technical Note, later in 2020.

TCFD Recommendations

The TCFD is a task force established by the Financial Stability Board with the aim of establishing a global framework for companies to disclose the impact of climate change on their business with the aim of helping investors to understand which companies are most at risk, which are best-prepared, and which are taking decisive action on climate change.

Its recommendations were published in 2017, and recommend clear disclosure on the impact of climate-related risks in the following areas of a company's business:

1. Governance: the organisation's governance around climate-related risks and opportunities;
2. Strategy: the actual and potential impacts of climate-related risks and opportunities on the organisation's businesses, strategy, and financial planning;
3. Risk Management: the processes used by the organisation to identify, assess, and manage climate-related risk; and
4. Metrics & Targets: the metrics and targets used to assess and manage relevant climate-related risks and opportunities.

In each category, the TCFD has recommended the specific topics to be described or disclosed, and it has provided additional general guidance and sector-specific guidance relating to financial companies (in particular, banks, insurance companies, asset owners and asset managers) and non-financial companies (energy, transportation, materials and buildings and agriculture, food, and forest products).

CP20/3 – Proposed New Disclosure Requirements

CP20/3 adopts the TCFD standards for disclosure wholesale. If adopted, UK premium-listed commercial companies (*i.e.*, companies subject to Listing Rules 9 and 21) will have to become familiar with these standards and report in accordance with them on a comply-or-explain basis.

The comply-or-explain approach is the standard required by the UK's Corporate Governance Code, and was adopted as the proposed standard for climate-related disclosure despite mixed feedback, as the FCA acknowledges that issuers' capabilities are still developing in some areas, and they may not yet have the data and capabilities to fully comply with certain of the TCFD recommendations, particularly those relating to scenario analysis and setting climate-related targets. The FCA also notes it does not want to be overly prescriptive at this stage, given the evolving nature of climate-related disclosure and modelling frameworks

CP20/3 – Guidance on Existing Climate-Related Disclosure Obligations

The other key element of CP20/3 is the proposed issuance of an FCA Technical Note to clarify *existing* climate-related and other environmental, social and governance ("**ESG**") disclosure. The FCA-proposed Technical Note is aimed at all issuers subject to existing EU legislation and rules contained in the FCA Handbook (*i.e.*, all issuers with securities listed on the London Stock Exchange, not just those in the premium-listed segment to whom the proposed rule on TCFD disclosure will apply).

It reminds those issuers that even where climate-related risks are not mentioned by name, they may still be important, and required to be disclosed under more general disclosure and internal controls obligations. For example, this proposed Technical Note will advise issuers that their existing obligations under the Listing Rules, the Prospectus Regulation, the UK Corporate Governance Code, the Disclosure and Transparency Rules, and the Market Abuse Regulation, may all involve a review of climate-related risks and, if necessary, related disclosure.

Conclusion

The TCFD's framework encourages businesses to face and evaluate the financial risk that climate change poses to their business, both in terms of physical risk posed by extreme weather and its consequences, and the "transition risk", meaning the large category of risks posed by behavioural changes as well as policy changes related to mitigating climate change. The TCFD framework has the aim of moving towards helpful, comparable disclosures related to these risks. This should allow investors (and consumers and regulators) to add a new dimension to their assessment of companies, and modify their behaviour accordingly.

Investors across the board agree that ESG factors are now routinely incorporated into mainstream investment decisions, and companies are required to demonstrate their insight and oversight on these topics. It is still not the case that a single framework dominates reporting on these matters, but this consultation paper shows that the TCFD framework will continue to grow in importance, at least in the UK. The FCA believes its proposals in CP20/3 are consistent with the UK Government's Green Finance Strategy, published in July 2019, and is a first step towards the adoption of the TCFD's recommendations more widely within the FCA's regulatory framework.

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If you have any questions, please feel free to contact any of the following Cadwalader attorneys.

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