Mirova response to the TCFD Consultation

Mirova is a subsidiary of Natixis Asset Management (BPCE Group), fully dedicated to responsible investment, with $7 billion of assets under management. Mirova appreciates the opportunity to comment on the Task Force on Climate-related Financial Disclosure (TCFD) report consultation relative to recommendations on climate-related financial risk disclosures.

1) Support for the TCFD's approach

- **Mirova supports the TCFD's approach and shares its observations**:
  - One of the essential functions of a financial market is to price risks and opportunities to support informed and efficient capital-allocation decisions. Without the right information, a misallocation of capital is likely to occur;
  - One of the most significant risks that issuers face today is climate change-related risks;
  - Investors need reliable, comparable and meaningful data on climate risks and opportunities in order to better make decisions.
  - Climate-related information should be released by corporates at a worldwide level.
- **Mirova also supports the objectives and scope set by the TCFD, i.e:**
  - To help identify the information needed by investors, lenders and insurance underwriters to appropriately assess and price climate-related risks and opportunities;
  - Ultimately, to facilitate authorities' assessment of the materiality of any risks posed by climate change to the financial sector.

2) General observations

- **The more complex the information requested, the more difficult to analyze and aggregate**
  - The level of complexity of some of the requested information often seems high, especially for sector-specific recommendations. Moreover, it is unlikely to envisage that this information will be gathered, aggregated and used by financial regulators in the short and medium run.
  - The information requested in addition to the published information is consequently too large and may discourage companies from producing the information requested, particularly in jurisdictions where the requirements for climate information production are still low or non-existent.

- **The French regulation is overall already consistent with most recommendations of the TCFD.** For Mirova, the main challenge for the TCFD will be the implementation of climate-related disclosure, at the international level across countries and industries.

- **Assessing physical and transition risks according to different standards:**
  - A distinction should be drawn between physical and transition risks. These two risks are provided the same level of importance in the TCFD's recommendations, whereas they are in fact of a distinct nature As such, they should not be evaluated by the same actors.

    - Physical risks
      - For corporates, these risks are tangible and linked to the location and climate-resilience of their physical assets. They can be assessed under the 2°, 4° and 6° IPCC (Intergovernmental Panel on Climate Change) scenarios but only thecompany/ the issuer, or a third party with access to very issuer-specific information - will be able to assess the physical risks of an issuer.
      - For the financial sector, they correspond to the financial translation of a potential aggravation of the effects of climate change.

- Transition risks
  - For corporates transition risks are more prospective and correspond to an estimate of the financial cost / viability of the business model of the company according to the potential climate scenario. They should not be evaluated by the company itself. To borrow an example from the world financial ratings; companies are not asked to rate their own solvency viability, but hire external third parties, so as to ensure that the information is reliable. Issuers should not be "judge and jury".
  - For the financial sector, exposure to transition risks does not differ in nature from the classical risk of financing non-viable assets in a rapidly changing economy. This corresponds more or less to the share of carbon-intensive assets (or highly carbon dependent assets) in the portfolios of banks and asset managers.

- **Direct publication by issuers of financial impacts based on heterogeneous methodologies could also mask the actual levels of risk** lying behind uncertain financial information.

- **Scenario analyzes may be too complex to implement and not prove necessary**
  - The practice of scenario analysis is a positive starting-point for favoring a better anticipation of climate change risks by companies;
  - However, directly requesting companies to publish scenario analysis on such complex issues, without reference scenarios and with different time horizons, may lead to the publication of even more heterogeneous, complex, unreadable or comparable information for investors, which would run contrary to the objectives of the TCFD.
  - Scenario analysis may not prove necessary to analyze the level of risk exposure of a company.

- **Beyond information issues**
  - Information is key for investors and regulators; however harmonizing climate-related disclosure will be a lengthy process. In addition, even if climate disclosure guidelines were well implemented at the international level, market information will never be perfect. The objective of harmonizing company publications – i.e. the aggregation of climate-related information provided by companies – is highly desirable, but is not something we see as feasible to be completed in the short and medium run. The role of intermediaries to analyze information provided by issuers is thus an important aspect, not sufficiently taken into account by the TCFD report.
  - A satisfactory amount of information will not suffice to protect the global financial system from climate-related risks: there are no reasons to believe that the market will be able to integrate this information in an efficient way. Preventing systemic risks also means an adequate capital allocation to ensure the implementation of the energy transition and the prevention of physical risks. This will require regulatory or fiscal incentives. Although no cost assessment of transition risks is available, the cost of non-financing the energy transition could be at least of 5% of the world GDP[1] with potential destabilizing consequences that may prove much more important than transition risks for the world financial system, climate scientists estimate that the true costs of climate change could far exceed the figures of the Stern Review.

[1] Stern, Nicolas. *Stern Review on the Economics of Climate Change*. Rep. London: UK Government, 2006. Print. The figures presented in the initial report were commented as being under-estimated in January 2013 by Nicholas Stern (https://www.theguardian.com/environment/2013/jan/27/nicholas-stern-climate-change-davos)

3) General recommendations

Mirova's everyday business as an asset manager fully dedicated to invest into sustainability has enabled our research team to draw on its experience to formulate additional observations that we hope will be of interest for the TCFD:

- **For a successful implementation, climate-related disclosure should be both meaningful and limited in quantity in order to be useful:**
    - There is an elevated risk of producing regulations that require high levels of climate disclosure that will be both costly to produce, yet ineffective in supporting sustainable investment decision-making. Excessive complexity in disclosure obligations could hamper the success of the TCFD's recommendations if companies are unable to disclose comparable and understandable information at a reasonable cost and/or if investors are not able to actually use this information as a basis for decisions and capital allocation;
    - The progressive integration of this information into financial reports to ensure control over production and disclosure is commendable, but may prove difficult and could be implemented progressively and prioritizing the most carbon-intensive sectors.

- **Information disclosure and analysis should be distributed among different actors in the framework of an ecosystem; an important role should be given to intermediaries between companies and investors:**
    - The role of the intermediaries to guarantee the quality and usefulness of data is key and should be strengthened. Information analysis should not rely on issuers; it is necessary to implement a proper information chain.
    - We believe the TCFD should promote the role of third-parties to ensure:
        - Data reliability and issuer verification by auditors;
        - Data analysis and risk assessment by financial or non-financial rating agencies or consultants;
        - The financial translation of climate-related risks and data comparability.

- **Analysis of scenarios by companies should be limited to physical risks and to the current situation of the company's business :**
    - We recommend that companies restrict themselves to the analysis of physical risk scenarios based on the 3 IPCC scenarios identified by the TCFD: 2° C, 4° C and 6° C.
    - In order to limit the number of variable, those scenario should be analyzed in the light of the current situation of the company and not on the basis of short-, medium- and long-term projections of the company's strategic and financial planning.
    - The results of these analysis should be published in the metrics and targets section of the report.

- **Assigning the analysis of transition risks to third-party intermediaries:**
    - We recommend that the transition risk scenarios associated with the IEA's scenarios (1.5 °C, 2° C, and 3.6° C) be analyzed by external third parties as part of issuer ratings and evaluations.

- **Disclosure for the financial sector:**
    - Guidelines should focus more on the systemic risk posed by not participating in the financing of the energy transition. Article 173 VI of the French "law on the financing of the energy and ecological transition" requires that the financial sector explain how it contributes to the financing and implementation of national and international climate objectives. (see in appendix our comments on disclosure guidelines for the financial sector)

- **Non-financial sector-specific guidelines**
  - We do not consider it necessary to issue specific recommendations for these sectors. If the magnitude of the numbers and the stakes are much higher for these sectors, the nature of the information does not differ.
  - Guidelines should only insist on requesting the publication of information related to scope 3 emissions and avoided emissions for GHG-intensive sectors and provide appropriate methodological support for these two indicators.
  - The Materials and buildings sectors are aggregated within the framework of the recommendations of the TCFD while they do not cover the same operational realities. We recommend that these two sectors be treated separately.

4) Mirova's comments and recommendations on the general TCFD disclosure recommendations:

We agree with the overall structure of the report, however the strategy section should be simplified, and the metrics and targets section should be both reinforced and simplified.

- **Governance:**
  - We believe that section captures all the essential elements with regards to how an organization's board addresses climate-related risks and opportunities.
  - Furthermore, we commend the TCFD's addition of a disclosure on climate-related performance remuneration schemes.

- **Strategy:**
  - We recommend that the organization of this section be implemented in a simpler fashion. This will make it more approachable for the readers and easier to use by investors. We also recommend connecting this section with the metrics and targets section.

    - Description of risks and opportunities:

      We recommend using the risks of each entity as a starting point, and to distinguish between:

      - The risks and opportunities related to the business / offer (product or service) of the company
        - Green vs. carbon products and services
        - Green vs. carbon research & development
      - Risks and opportunities related to the production process
        - The supply chain and/or value chain
        - Operations
        - Adaptation and mitigation activities

In our opinion, it is unnecessary and too complex to ask issuers to project these risks in the short, medium and long term, but simply to estimate the issuer's risk mapping.

- **Risk management:**
  - We believe this section captures the main information needed to be disclosed with regards to how an organization integrates climate-related risks into its risk management process. It would be interesting to have information on how the company also identifies and manages climate-related opportunities.

- **Metrics and targets:**
  - Mirova agrees that investors need to be able to understand how issuers measure and monitor their climate-related risks and opportunities. We believe that this section should be both simplified and strengthened and focus only on the following information.

- **Level 1:** For reporting purposes, we believe the TCFD should recommend the provision of the level of firm green/fossil exposure, and of its targets;
  - Revenue
  - EBITDA (in the case of utilities)
  - Investments
  - R&D
- **Level 2:** Current emissions and targets
  - We believe that scope 1, 2 and 3 are always relevant to include in any climate-related disclosure, even if they happen to be low. Scope 3 should therefore always be included;
  - Another addition should involve the emissions avoided, especially in the case of CO_2 intensive industries;
- **Level 3:** Physical risks scenarios
  - The impact of the risks of each scenario (2° C, 4° C and 6° C), adjusted for the current parameters of the company, should be taken into account,
  - This should include relevant figures on:
    - Input costs
    - Operating costs
    - Revenues
    - Supply chain
    - Business interruption

Lastly, all published figures should be accompanied by comments, and all published indicators should be the subject of methodological explanations, if necessary in a separate document.

APPENDIX

For the banking, insurance and asset owner businesses, we have summarized what we find to be both relevant and not relevant in the TCFD's recommendations:

Banking sector:

The information that we consider useful:

- **Strategy**: The concentration of credit exposure to carbon-related assets. In addition, banks should present how they wish to refocus their activity on low-carbon assets, and help reduce the physical risks associated with climate change by financing the energy transition;

- **Metrics and targets:** Amount and percentage of carbon -relative assets relative to total assets as well as the amount of lending and other financing connected with climate-related opportunities**.**

The information that we consider to be too complex to gather:

- **Risk management:** Characterizing climate-related risks as traditional banking industry risks (credit risks, market risk, liquidity risk, operational risk
- **Metrics and targets:** Assess the impact of physical and transition climate-related risks in the short, medium and long term, broken down by industry, geography, credit quality and average tenor.

Insurance sector:

The information that we consider useful:

- **Strategy:** Potential impacts of climate-related risks and opportunities on their [strategies], (...) core businesses, products and services (...); How it influences client and broker selection, and whether specific climate-related products or competencies are under development (...).

- **Metrics and targets:** Insurance companies should provide aggregate risk exposure to weather-related disasters of their property business by relevant jurisdictions.

The information that we consider to be too complex to gather:

- **Strategy:** impact of different scenarios] Description of the climate-related scenarios (...) [on their underwriting activities].

- **Risk management:** Insurance companies should describe the processes for identifying and assessing climate-related risks on re / insurance portfolios by geography

- **Risk management:** Insurance companies should describe key tools or instruments used to manage climate-related risks in relation to product development and pricing (...)

Asset owners:

The information that we consider useful:

- **Strategy:** Description of impacts of risks and opportunities] Asset owners should describe how climate-related risks and opportunities are factored into relevant investment strategies. This could be described from the perspective of the total fund or investment strategy or individual investment strategies for various asset classes.
- **Risk management:** Asset owners should describe, where appropriate, engagement activity with investee companies to encourage better disclosure and practices related to climate-related risks to improve data availability and asset owners' ability to assess climate-related risks.
- **Risk management:** Asset owners should describe how they consider the positioning of their total portfolio with respect to the transition to a lower-carbon economy […]. This could include explaining how asset owners actively manage their portfolios' positioning in relation to this transition.
- **Metrics and targets (a):** Asset owners should describe metrics used to assess climate-related risks and opportunities in each fund or investment strategy. (…) Where appropriate, asset owners should provide metrics considered in investment decisions and monitoring.
- **Metrics and targets (b): scopes 1, 2 & 3:** Asset owners should provide GHG emissions, where data are available, associated with each fund or investment strategy normalized for every million of the reporting currency invested.

The information that we consider to be too complex to gather:

- **Strategy (c):** description of scenarios on the organization] Asset owners that perform scenario analysis should provide the following: a discussion of how climate-related scenarios are used, such as to inform investments in specific assets, and description of climate-related scenarios used and associated time frames.

Asset managers:

The information that we consider useful:

- **Strategy:** Asset managers should describe how climate-related risks and opportunities are factored into relevant products or investment strategies. Asset managers should also describe how each product or investment strategy might be affected by the transition to a low-carbon economy.

- **Risk management:** Asset managers should describe, where appropriate, engagement activity with investee companies to encourage better disclosure and practices related to climate-related risks (…).

- **Risk management:** Asset managers should also describe how they identify and assess material climate-related risks for each product or investment strategy. This might include a description of the resources and tools used in the process.

- **Risk management:** Asset managers should describe how they manage material climate-related risks for each product or investment strategy.

- **Targets and metrics:** Asset managers should describe metrics used to assess climate-related risks and opportunities in each product or investment strategy. Where relevant, asset managers should also describe how these metrics have changed over time. Where appropriate, asset managers should provide metrics considered in investment decisions and monitoring.

- **Targets and metrics scope 1, 2 and if appropriate scope 3:** Asset managers should provide GHG emissions, where data are available, associated with each product or investment strategy normalized for every million of the reporting currency invested.

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