5-13 New Street G/F
Sai Ying Pun, Hong Kong
+852 3905 2899
info@cdp.net www.cdp.net

July 30th, 2021

Re: CDP Submission on PPG 229: Climate Change Financial Risks

Dear [redacted],

CDP welcomes the opportunity to comment on the draft PPG 229 Climate Change Financial Risks, and we commend APRA for developing the PPG in recognition of the relevance of climate-related risks to the stability of Australia's financial system. Our overall impression is that the proposed PPG represents a bold step forward in fostering a more climate-resilient financial system for Australia.

We are pleased to offer the feedback below from our perspective as a global non-profit that runs the world's environmental disclosure system for companies, cities, states and regions. Founded in 2000 and working with over 590 investors with $110 trillion in assets, CDP pioneered working through capital markets and corporate procurement to motivate companies to disclose their environmental impacts, and to reduce greenhouse gas emissions, safeguard water resources and protect forests. Over 10,000 organisations around the world disclosed data through CDP in 2020, including more than 9,600 companies worth over 50% of global market capitalisation, and over 940 cities, states and regions, representing a combined population of over 2.6 billion.

Fully TCFD aligned, CDP maintains the largest environmental database in the world. CDP scores are used to drive investment and procurement decisions towards a zero-carbon, and resilient economy. CDP data powers the global ESG ecosystem and is incorporated into platforms and outlets like Bloomberg, MSCI, DJSI, and Euronext, among others. CDP is also a founding member of the Science Based Targets initiative, the We Mean Business Coalition, the Investor Agenda and the Net Zero Asset Managers initiative.

Based on our experience working with financial institutions and regulators worldwide, I would draw your attention to the following key messages from our comments below. We would respectfully ask APRA to consider amending the PPG to:

- Encourage regulated entities to develop transition plans and to put these plans before shareholders at AGMs
- Encourage regulated entities to measure and report portfolio emissions using the PCAF methodology and to incorporate these emissions into climate targets
- Clarify expectations with respect to conducting and reporting the results of scenario analysis
- Clearly identify TCFD reporting as the primary disclosure framework

We propose these amendments in order to ensure that the PPG will present regulated entities with the guidance necessary to provide the capital markets with comparable, decision-useful data. To that end, we have indicated the frameworks, standards, and other reference points which our stakeholders have found most useful in enabling financial institutions to meet global best practices. Our feedback is also intended to bolster the synergies between the PPG and the position expressed in the recent G7 communique, endorsed by Australia, calling for mandatory, TCFD-aligned climate-related disclosure[1].

CDP questionnaires capture company performance across the four pillars of the TCFD, and our comments draw on data contained in climate disclosures submitted to CDP by over 330 financial institutions in 2020, among which were 16 Australian institutions (including the big four banks and largest insurance companies). The number of disclosing entities is expected to grow significantly by the end of CDP's 2021 disclosure cycle. We would be happy to provide relevant data to APRA at no cost. We would also welcome further discussion on how our disclosure system and data may be useful to APRA in monitoring the implementation of the PPG.

For further context on the climate-related risks and opportunities identified by financial services companies responding to CDP, please see our report The Time to Green Finance. Additional recommendations for policymakers and regulators to incentivize corporate climate action are captured in the recent brief The Time for Action is Now. We would also direct you to the report Confusion to Clarity, developed in partnership with IGCC and PRI, for more on the significance of TCFD reporting in Australia.

Please find CDP's full submission on PPG 229 below. We have focused on the sections of the guidance where we felt that our expertise would be most useful to your team. Please feel free to get in touch should you wish to follow up on any of our comments. We look forward to further engaging with APRA.

Yours,

[redacted]

[redacted]
Director – Hong Kong, Southeast Asia, Australia and New Zealand
CDP

[1] G7 (2021): Carbis Bay G7 Summit Communique.

APPENDIX: CDP Submission on PPG 229: Climate Change Financial Risks

Governance

This section contains much useful guidance, and we echo APRA's comments on the importance of assigning the responsibilities identified in Paragraph 17 to the senior management team. Items A through D enumerate the actions of an engaged senior management team that is well positioned to discharge its responsibilities.

In recognition of the importance of these responsibilities in prudential management, we would ask APRA to consider putting these responsibilities in the context of executive remuneration. As management of climate related risks and opportunities plays a key role in an institution's long-term performance, executive remuneration should incentivize the effective implementation of climate strategy. This is particularly urgent, as CDP data indicates that just 21% of financial institutions responding to CDP report incentivizing portfolio alignment to climate-related objectives[2].

Any disconnect between remuneration incentives and actions to align portfolios with climate-related objectives is especially significant from an accountability perspective. It is relevant to depositors, policyholders, and superannuation fund members to understand how executive remuneration aligns with the successful implementation of climate-appropriate strategies. We would therefore encourage APRA to indicate that a prudent institution would link climate-risk management and apply climate-related metrics to the performance-based component of executive remuneration packages as applicable.

CDP also agrees with APRA's position that it is vital for boards to exercise oversight with respect to climate-related risks and opportunities, as laid out in paragraphs 13 to 16 of the PPG. A recent review of 332 financial institutions responding to CDP's financial services questionnaire found that almost all financial institution reporting to CDP report some degree of board-level oversight of climate-related issues[3], and this is to be encouraged among APRA-regulated institutions.

However, the same review also found that board-level oversight covers climate-related issues in financial institutions' own operations more often than it covers issues relating to the institutions' financing activities. While this trend appears across all financial service activities, it is most stark for insurance companies, only 31% of which report board-level oversight of the climate-related impacts of their underwriting activity[4].

This lack of attention is particularly concerning since financial institutions' major climate-related risks, opportunities and impacts occur in their financing portfolios. The review of CDP responses from financial institutions indicates that only 25% of disclosing entities

---

[2] CDP (2020): The Time to Green Finance.
[3] Ibid
[4] Ibid

report portfolio emissions. Among those that do, portfolio emissions are on average 700 times higher than their direct accountable emissions[5]. Given the scale of financed emissions compared to direct emissions, financed emissions should be given adequate time and attention by boards, at least as much attention as operational concerns related to climate change, and ideally more.

The lack of transparency around portfolio emissions has troubling implications beyond the performance of individuals financial institutions. The Network from Greening the Financial System, among others, has identified unaccounted for climate risk as a threat to the stability of the financial system as a whole[6] and recommended that supervisors require regulated entities to identify vulnerabilities to climate related risks, which entails accounting for financed emissions[7]. In this vein, supervisors like the Hong Kong Monetary Authority[8] and the United Kingdom's Financial Conduct Authority[9] have indicated that they intend to include measurement of portfolio emissions within their guidelines. We would therefore suggest that APRA consider expanding the scope of prudential board oversight to consider financed emissions.

We would also propose that APRA advise regulated entities to develop and disclose their plans to transition to a low-carbon economy. Although transition planning is an essential, forward-looking tool, both CDP analysis[11] and the TCFD's 2020 status report indicate that levels of forward-looking disclosure remains low[12]. Still, 49% of financial institutions responding to CDP report that they have a low-carbon transition plan, indicating that leading financial institutions are preparing for a net-zero future[13]. Clear guidance from APRA on transition planning could help to level the playing field and provide the impetus for regulated entities to design credible transition plans. As we discuss in further detail in our comments on disclosure below, regulated entities can use the framework for financial services companies developed by the Science-based Targets Initiative (SBTi) to develop viable, expeditious transition plans.

[5] Ibid
[6] NGFS (2020): A Status Report on Financial Institutions' Experiences from working with green, non green and brown financial assets and a potential risk differential.
[7] NGFS (2020): Guide for Supervisors: Integrating climate-related and environmental risks into prudential supervision.
[8] HKMA (2020): White Paper on Green and Sustainable Banking.
[9] FCA (2021): Enhancing climate-related disclosures by asset managers, life insurers, and FCA-regulated pension providers.
[11] CDP (2020): The Time For Action Is Now.
[12] FSB (2020): 2020 Status Report: Task Force on Climate-related Financial Disclosures.
[13] CDP (2020): The Time For Action Is Now.

To formulate relevant guidance, APRA could draw on globally accepted principles for effective transition planning. CDP acknowledges the Oxford Martin Net Zero Carbon Investment Initiative, according to which companies should[14]:

- Commit to a timeframe to reach net-zero emissions in line with the Paris goals;
- Demonstrate that they will be able to continue to be profitable once they reach net-zero emissions; and
- Set quantitative mid-term targets to be able to demonstrate progress against their long-term goals

Adopting this or a similar set of principles would ensure that the capital markets are provided with information required to understand whether financial institutions are taking necessary steps to thrive in a net-zero economy.

Building on this, APRA may wish to consider encouraging entities to put transition plans before shareholders for a vote. Shareholder votes on transition plans at annual general meetings (AGMs) both increase accountability and expedite the shift toward a low-carbon future. Maintaining transition plans as a scheduled AGM item allows shareholders to review progress and raise resolutions as appropriate. This in turn allows shareholders and other stakeholders to assess the institution's soundness in a net-zero economy. APRA-regulated entities can refer to the Say on Climate Campaign, which offers resources for developing resolutions on transition planning, for further guidance.

Starting this year, CDP asks financial institutions to report on transition plans. Companies that have a transition plan are asked to report whether their plans are a scheduled AGM item. These companies can also provide additional details about their transition plans. Companies that do not currently publish transition plans can disclose plans to do so. Responses to these questions will be available to the public and for free on CDP platforms in late 2021.

Risk management

CDP applauds the solid guidance provided in this section of the PPG. We agree that both quantitative and qualitative information is necessary to provide stakeholders with a complete picture of entities' exposure to climate-related risk, and we further support the conclusion regulated entities will likely have to engage with a variety of stakeholders – customers, suppliers, external experts, and other counterparties, for example – in order to carry out comprehensive risk monitoring.

We would suggest expanding the guidance around emissions reporting, specifically with respect to Scope 3 emissions. While existing legislation (namely, the National Greenhouse Gas Reporting Act of 2007) requires high-emitting companies to report their Scope 1 and Scope 2 emissions, CDP is not aware of any measures that require

[14] Oxford Martin School (2018): The Oxford Martin Principles for Climate-Conscious Investment.

Australian companies to report their Scope 3 emissions. APRA is well placed to address this gap by sending a strong signal that prudent risk management requires an awareness of emissions embedded throughout the value chain. This is especially important given the outsized role that Scope 3 emissions – specifically financed emissions – play in most financial institutions' overall emissions profile.

Although CDP data indicates that reported portfolio emissions are on average 700 times greater than financial institutions' operational emissions, only 51% of financial institutions reported analyzing their portfolio impacts, and just 25% disclosed their financed emissions. The lack of data and transparency suggests that financial institutions have yet to give sufficient attention to their portfolio emissions, even though almost all of their climate risks and impacts are driven by the activities financed.

Given both the scale of the emissions involved and inadequate data coverage on portfolio impacts, APRA should consider explicitly stating that a prudent financial institution would measure and report its Scope 3 emissions, giving special attention to adequate measurement and disclosure of financed emissions.

Guidance on measuring and reporting portfolio emissions could refer to the Global GHG Accounting and Reporting Standard for the Financial Industry developed by the industry-led Partnership for Carbon Accounting Financials (PCAF), a global partnership of financial institutions that has developed a harmonized approach to measuring and reporting financed emissions[17]. PCAF's methodology for calculating and reporting financed emissions builds on the Corporate Value Chain (Scope 3) Accounting Standard developed by the GHG Protocol, the leading methodology for Scope 3 measurement. PCAF is also referenced in TCFD guidance.

As a result of these linkages, PCAF has become a mainstream tool in portfolio emissions accounting, with over 140 financial institutions – banks, asset owners and managers, insurance companies, and others – using PCAF's GHG accounting standard to measure and report financed emissions[18]. APRA may wish to consider revising the PPG to include specific reference of PCAF in order to help regulated entities remain aligned with global best practices in measuring and reporting financed emissions.

In addition to identifying risks embedded in a financial institution's portfolio, measuring financed emissions plays a critical role in setting meaningful targets. PCAF is again relevant in this context, as its methodology is aligned with the targeting framework for financial institutions developed by the Science-based Targets Initiatives (SBTi) in 2020[19]. Setting net zero-portfolio targets and other targets aligned with the Paris Agreement has become a central focus among financial institutions, as evidenced by the establishment and growth of initiatives like the Net Zero Asset Managers Initiative and the UN-convened Net Zero Asset Owners Alliance and Net Zero Banking Alliance.

---

[17] PCAF (2021): The Global GHG Accounting & Reporting Standard for the Financial Industry.
[18] PCAF (2021): Financial Institutions Taking Action.
[19] SBTi (2021): Guidance: Science-based targets for the financial sector (updated April 2021 version).

Given the importance of target setting in both transition planning and in driving decarbonization generally, we would ask APRA to consider including guidelines on setting and disclosing climate targets with reference to the SBTi framework.

CDP currently collects extensive data on financial institutions regarding climate-relate targets. Future versions of CDP's sector-specific questionnaire for financial services companies will feature a standalone question requesting details about portfolio targets. This will allow financial institutions to provide stakeholders with relevant information in a standardized format and allow stakeholders to evaluate targets and track progress.

Scenario analysis

The section on scenario analysis contains strong, actionable advice. CDP agrees with APRA's position in Paragraph 39 that financial institutions should make a start with qualitative analysis and build capacity for quantitative analysis over time, without letting the perfect be the enemy of the good. CDP data indicates that only 57% of financial institutions report using scenario analysis[20]. Among companies not currently conducting scenario analysis, the majority indicate that they intend to do so within the next two years; clear guidance from APRA could help lagging institutions to expedite their process.

Paragraph 40 helpfully identifies leading practices in conducting scenario analysis, particularly with respect to the broad range of scenarios and elements recommended (orderly and disorderly; a full range of risks; various time horizons; etc). This summary present a valuable starting point for companies new to scenario analysis and the practices identified conform to investor expectations. Given the importance of robust scenario analysis in meeting stakeholder expectations, we would suggest that APRA strengthen the language around these leading places. For example, in 40(b)(i) and 40(b)(ii), the guidance indicates the types of physical and transition-related considerations that regulated entities "could" include in their analysis. We would suggest that APRA consider indicating that reporting entities *should* consider these factors, so as to more firmly underline the importance of comprehensive scenario analysis.

Furthermore, we note that in item 40(b)(i) on future temperature rise, the guidance suggests that warming of 2° is consistent with the goals on the Paris Agreement. In fact, the Paris Agreement has established a maximum temperature increase of 1.5° as a long-term goal. We would there suggest revising this section to underline that companies should use a 1.5° scenario in their analysis and design their transition plans accordingly.

APRA could consider providing additional guidance on conducting scenario analysis. CDP considers it best practice to select at least two scenarios for analysis, one physical scenario and one transition scenario[21]. We suggest that entities new to scenario

[20] CDP (2020): The Time to Green Finance.
[21] CDP (2021): CDP Technical Note on Scenario Analysis.

analysis select publicly available, peer-reviewed scenarios and use these as a starting point for developing their own organizational and business-specific scenarios. Suitable scenarios should be:

- Peer reviewed
- Used/referenced and issued by an independent body
- Supported by publicly available data sets, where possible
- Updated regularly
- Linked to function tools (e.g. visualizers, calculators, and mapping tools)

A partial list of scenarios meeting these criteria can be found the CDP's *Technical Note on Scenario Analysis.* APRA is welcome to mention this document among the other guidance material in Paragraph 42.

To increase transparency, in cases where companies elect to use bespoke models for scenario analysis, we would advise them to disclose input assumptions, comparisons, and any divergence from the standard set of assumptions.

Disclosure

We applaud the PPG's guidance around disclosure, and we appreciate that the PPG is not intended to create new disclosure requirements for regulated entities. Nonetheless, in reflection of the growing consensus on the importance of climate disclosure, we submit that it would be appropriate for APRA to lay out clearer expectations that regulated entities will adopt best practices in climate disclosure, even if these expectations are non-binding.

In Paragraph 48, we would ask APRA to consider more explicit guidance that prudent companies should reporting using the TCFD framework. Such guidance would echo broad support for the TCFD among companies, regulators, and the investment community. It would also ensure that Australian financial institutions are disclosing in line with the most widely accepted measurement practices, methodologies, and guidance. This in turn would ensure that regulated entities are reporting the most relevant, comparable data required for the stability of the financial system.

APRA could follow the example set by the Monetary Authority of Singapore[22] (MAS) and the European Commission[23] (EC), both of which have released guidelines on climate reporting that make clear reference to the TCFD as the leading disclosure framework. While both MAS and the EC acknowledge that their guidance is non-binding, the documents lay out each authority's respective expectations for prudent management of climate-related issues, including TCFD-aligned disclosure. A similar expression of

[22] MAS (2021): Regulations and Guidance: Risk Management/Environmental Risk. See individual guidelines for insurers, banks, and asset managers.
[23] EC (2019): Guidelines on reporting climate-related information.

support for the TCFD could provide regulated entities with the certainty needed to coalesce around the framework.

We would also invite APRA to consider referring regulated entities to CDP's climate change questionnaire, which is standardized and fully aligned with the TCFD recommendations, for reporting TCFD-relevant data. CDP provides a global platform for disclosing entities to collect and organize data and provide data to capital markets in a structured format. Our guidance materials help responding companies to identify relevant data for their reporting, and CDP scores allow benchmarking of regulated entities against peer organizations both within Australia and globally.

CDP continues to dialogue with the TCFD, most recently responding to the taskforce's recent public consultation on updating guidance for metrics, targets, and transition plans. Changes to the TCFD framework will be reflected in updates to our climate change questionnaire. Given that the proposed IFRS standards will be built on the TCFD recommendations[26], annual CDP reporting offers regulated entities a way to remain up to date on the best practices in reporting. The data disclosed through the CDP platform provides the regulators and the investment community with high quality, consistent, comparable, TCFD-aligned data at scale.

[26] IFRS (2020): Consultation Paper on Sustainability Reporting.