# The climate risk reporting journey

## A corporate governance primer

## A step-change in financial disclosure expectations

In late 2015, in the shadow of the Paris Agreement and amid increasing concerns of investors, regulators and other stakeholders about the financial implications of climate change, the G20 tasked its Financial Stability Board (**FSB**) to review how the financial sector could take account of climate-related issues. The FSB commissioned an industry-led taskforce: the *Taskforce on Climate-related Financial Disclosures* (**TCFD**), chaired by Michael Bloomberg. The TCFD was charged with developing a voluntary framework for companies to disclose the material impacts of climate change on their financial performance and prospects, in a consistent form, that would be decision-useful for investors, lenders and insurance underwriters. The TCFD released its final Recommendations in June 2017. Whilst 'voluntary', the TCFD Recommendations are emerging as the key benchmark against which to assess a company's strategic approach to the climate change mega-trend. However, many directors (and the executives on which they rely) are ill-prepared to navigate this step-change in governance and disclosure expectations.

## Reporting and assurance

The board's approval of financial statements, and the accompanying narrative directors' report, is a primary source of assurance to shareholders. In turn, directors must exercise due care and diligence in assuring that the company's disclosures present a true, fair and balanced view of financial performance and prospects, and that they have been prepared on the basis of a robust process. This requires the board to both understand key risk areas, and to satisfy themselves that effective controls are in place.

**This primer is intended to assist boards and their committees embarking on the climate-related financial risk reporting journey. It proposes key questions relevant to the assurance of a corporation's reporting on climate-related financial issues – and to the robust processes of governance and oversight on which those disclosures must be based.** Whilst recognising that the TCFD provides a framework for *reporting* rather than board governance *per se*, the primer seeks to place each query in context by indicating the category(s) of TCFD Recommendation to which they relate.

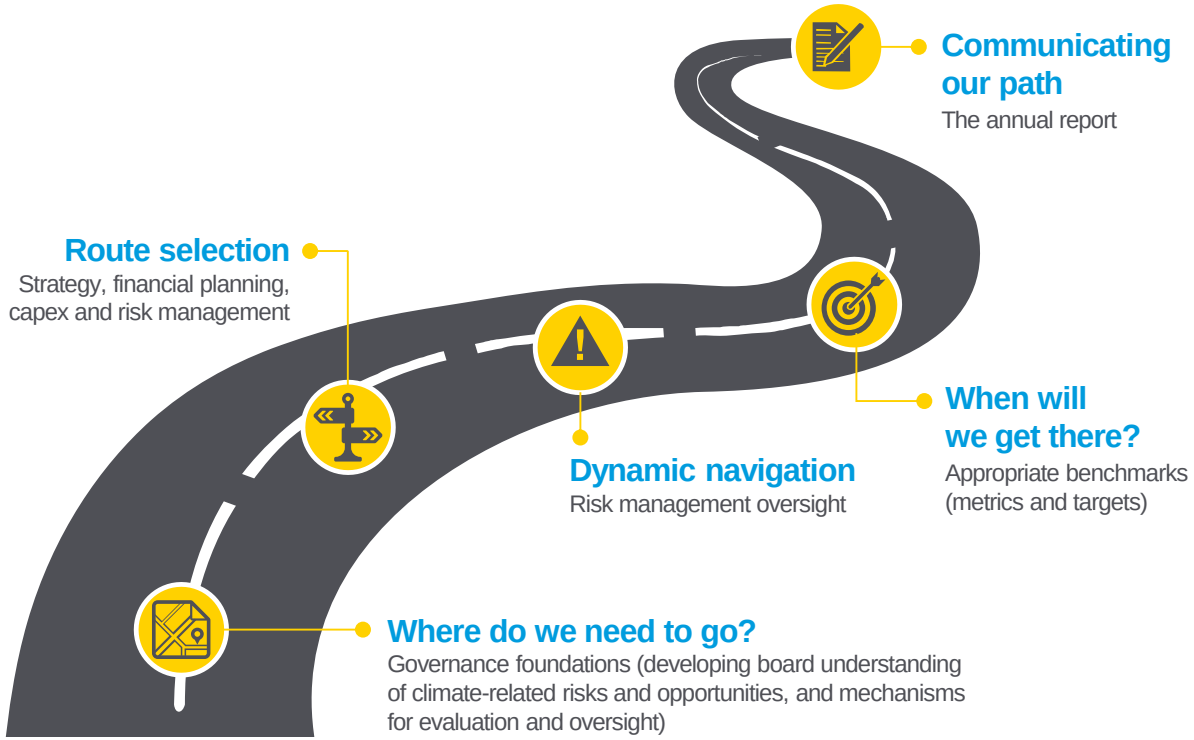


CENTRE FOR POLICY DEVELOPMENT

COMMONWEALTH Climate and Law Initiative

MinterEllison

The journey is broken down into a number of steps:




Of course, the actions required to discharge a director's obligations to govern climate-related risks (and opportunities) with due care and diligence, and to ensure that corporate reports present a true and fair view of financial performance and prospects, will be unique in each case. In particular, additional interrogation and assurance may be warranted in sectors with significant climate-related exposures (such as financial services, resources, energy, infrastructure, materials & manufacturing, transportation, agribusiness and real estate, amongst others). *Accordingly, this guide is high-level and general in nature only, and is not intended to provide or replace legal advice tailored to your specific jurisdiction and circumstances.*

Contact a member of the MinterEllison climate governance team (at the end of this primer) for assistance with climate risk assurance that is specific to your needs.



CENTRE FOR POLICY DEVELOPMENT

COMMONWEALTH Climate and Law Initiative

MinterEllison

# 1 Where do we need to go?

## Governance foundations (developing board understanding of climate-related risks and opportunities, and mechanisms for evaluation and oversight)

| | TCFD RECOMMENDATION CATEGORY | | | |
|---|---|---|---|---|
| | Governance | Strategy | Risk Management | Metrics & Targets |
| Have the board and senior management (including legal, governance, finance and risk teams) been briefed on climate-related risks (and opportunities) to enable us to discharge our obligations in relation to governance, strategy and risk management oversight? In particular, do we understand the different drivers (and consequences) of physical climate impacts (increase in both acute catastrophic and gradual onset) and economic transition-related risks (policy/regulatory (including under the Paris Agreement), technological, stakeholder) for our business? Do we understand the difference between climate change mitigation and adaptation? Do we understand the role of stress-testing and scenario analysis in strategic governance, planning and risk management? Do we understand any relevant exposures to stranded asset risk?<br><br>By whom are we being advised on these issues? How have we assured that their expertise is relevant and appropriate? What processes are in place to ensure that we remain informed of developments in this area? | ■ | ■ | | |
| How are issues associated with climate change integrated into our board governance (strategic and oversight) responsibilities? Is this issue receiving adequate time and focus within the board / committee agenda? | ■ | ■ | ■ | |
| In what part(s) of the business does operational responsibility for climate-related issues (identification, assessment, management and monitoring) reside? Who is responsible and accountable for this issue within management? Are we satisfied that relevant staff (or the experts that they consult) have the appropriate competence and resources? How is climate change integrated into our strategic reviews, capital and business planning, performance objectives and 'standard' risk management framework? How are relevant exposures, and progress against strategies and targets, monitored and assessed by management, and reported to the board or its committees (on both a regular and exceptions basis)? (*See further under Dynamic Navigation - Risk Management Oversight, below)* | ■ | | ■ | |
| Have directors updated their standing declarations to identify extraneous interests that may compromise their ability to exercise independent judgment on climate-related governance issues in the best interests of the corporation? | ■ | | | |
| Do climate change-related matters impact on our Directors' & Officers' insurances – from coverage exclusions and 'occurrences', to disclosure and notification considerations? | ■ | | | |

# 2 Route selection

## Strategy, financial planning, capex and material risk management

| | TCFD RECOMMENDATION CATEGORY | | | |
|---|---|---|---|---|
| | Governance | Strategy | Risk Management | Metrics & Targets |
| What foreseeable climate-related risks (and opportunities) are relevant to our sector(s) and geographic location(s) – not only within our business fence-lines, but upstream in our supply chain and downstream in our distribution chains? Are there any factors that compound (or mitigate) our enterprise risk exposures vis-à-vis other companies in our sector(s)? | | ■ | ■ | ■ |
| How does our exposure differ under stress-testing against a range of plausible climate futures (including one aligned with Paris Agreement goals to keep average warming *'well below'* 2C), over various time horizons relevant to our business and investment planning and useful asset life-cycles (short, medium and long-term)? On what basis do we believe these scenarios represent an adequate range of credible physical, economic transition and litigation risks (and opportunities) that could reasonably be expected to impact on our business performance or prospects? | | ■ | ■ | ■ |
| Which of those risks present a *material* exposure to our corporate strategy or operations (in both absolute and relative terms) – and on what basis is the threshold of 'materiality' set? Over what time frames? | | ■ | ■ | ■ |
| What are the key climate-related scenarios, variables and assumptions in this strategic analysis (including forward-looking stress testing)? On what basis have these input parameters been selected as appropriate? How do the outcomes vary under a range of different, albeit plausible, assumptions? | | ■ | ■ | ■ |
| What are the implications of identified material climate risks and opportunities for our business model? What strategic responses are open to us to continue to thrive – stress-tested against a range of potential climate futures (*as above*)? This should include both a strategic response to potential market shifts (external impacts), and an operational response to lower our own exposure to climate-related risks (including, but not limited to, emissions mitigation strategies as against science-based targets) (internal responses). What does it mean for our product/services offering, R&D investment, M&A, capital allocation and cost of finance? Is our strategy clearly articulated, and has it been reviewed/approved by the board and/or its committees (as appropriate)? | | ■ | | |
| What corporate policy(s) do, and should, we have in place in relation to climate change and its impacts? Does this policy align with Paris Agreement goals and/or science-based emissions reduction targets? Why/why not? How is this policy reflected in our procurement and other contracting practices? | | ■ | ■ | ■ |
| What are the metrics and targets against which we measure our exposure to (and assess our progress in managing) climate-related risks, including (but not limited to) absolute and intensity-based emissions reduction targets? Over what time frames, and against which base year? Why are these parameters relevant and appropriate? What are our key performance indicators against those targets? | | ■ | ■ | ■ |
| What events or developments should trigger our reassessment of such risks and/or a shift in strategic trajectory? What signposts do we monitor to gauge whether our central (and other) case assumptions require revision? What are the trigger points for our re-assessment of these issues? How, and how often, do we re-calibrate relevant signals? | | ■ | ■ | ■ |

# 3 Dynamic navigation

## Risk management oversight

&

# 4 When will we get there?

## Metrics and targets

| | TCFD RECOMMENDATION CATEGORY | | | |
|---|---|---|---|---|
| | Governance | Strategy | Risk Management | Metrics & Targets |
| What are the key climate-related variables and assumptions, and metrics and targets, that we apply? Why are these the appropriate parameters/benchmarks? How do the outcomes vary under a range of different, albeit plausible, assumptions? | | ■ | ■ | ■ |
| Have our variables, assumptions, parameters, benchmarks and methodologies been updated to reflect scientific, economic and financial developments (although recognising that these may be held constant for the purposes of meaningful trend analysis)? What impact do these developments have for our strategy, risk management and disclosure? | ■ | | ■ | ■ |
| How does management determine the order of priority to be given to each relevant climate-related risk/opportunity? | | | ■ | |
| What assessments of remuneration structures have been conducted to ensure that no perverse incentives exist that may undermine our policies or progress (eg. that may favour capex/investment in assets at risk of being stranded)? Conversely, have we considered revision of our remuneration policies to reflect progress against climate-related business objectives? | ■ | | ■ | ■ |
| How do we engage with, or otherwise seek to influence, stakeholders (employees, government, suppliers, customers) on climate-related issues? Have we considered whether our external associations, activities and engagements (such as membership of industry groups and/or government lobbying activities) may be perceived as inconsistent with our corporate climate change policy and/or disclosures? | ■ | ■ | ■ | |



CENTRE FOR POLICY DEVELOPMENT 10TH ANNIVERSARY

COMMONWEALTH Climate and Law Initiative

MinterEllison

# 5 Communicating our path

## Are annual report disclosures complete, accurate and reliable?

| | TCFD RECOMMENDATION CATEGORY | | | |
|---|---|---|---|---|
| | Governance | Strategy | Risk Management | Metrics & Targets |
| Is our industry identified as one at 'high risk' in the TCFD Recommendations? Have our annual reports been prepared with regard to the TCFD (or other recognised frameworks such as SASB, GRI/IIR, CDSB etc)? *If not, why not – particularly if we are in a high-risk industry?* If so, what is the process by which our reports have been reconciled or assured against the relevant framework(s)? | ■ | ■ | ■ | ■ |
| Can management provide a brief overview of the process for preparing the financial statements, explanatory notes, directors' report (eg. the Operating & Financial Review (**OFR**)) and corporate governance statements, including the review processes? What has made management (and, independent of management, our external auditors) confident about the accuracy and integrity of the information reported as it relates to the impact of climate change on our performance and prospects? What are the key assumptions made, and metrics or statements requiring the most judgment? In what areas did our external auditor disagree with or challenge positions taken by management? Were any climate risks issues raised as key audit matters? What steps have been taken with regards the auditor's responsibility relating to other information to ensure consistency between financial and narrative disclosures? | ■ | | ■ | |
| How have any material impacts of climate change on our financial position been assessed (eg. asset valuation or impairment, liability provisions, revenues, expenditures, and cash flows)? In particular, what methodology has been applied in impairment testing of material assets? Are these reasonable and supportable? Are particular disclosures of key assumptions and uncertainties warranted? Do we need to adjust asset recognition, reported valuation or relevant liability provisions to account for our assessment of stranded asset risks? Should we be disclosing our Scope 1, 2 and/or 3 emissions (in line with GHG Protocol Methodology), on an absolute and/or intensity basis (eg. emissions efficiency by unit of output)? Why/why not? | ■ | | ■ | ■ |
| What range of climate-related assumptions, scenarios and potential material financial impacts have been considered by management but not disclosed? On what basis has it been determined that they should not be disclosed? Are we proposing to disclose only favourable scenarios? How do reported performance and prospects vary under a range of different, albeit plausible, assumptions? Is it appropriate to disclose the nature of the material variables that may impact on the relevant outcome ('modifying factors'), and a description of our methodologies? *Directors may ask management and/or investigating accountants to provide a due diligence report that outlines the procedures followed, inquiries undertaken, supporting/verification information and conclusions reached.* | ■ | | ■ | ■ |
| What forward-looking statements in relation to the risk (and opportunities) associated with climate change for our financial prospects are appropriate to disclose to the market (including in the directors' report/OFR)? Are any such statements reasonable and supportable, and grounded in stress-testing and scenario planning in relation to both physical and economic transition-related risks, over time-horizons consistent with our capital and financial planning cycles? Does that disclosure accurately convey the potential for materially different outcomes depending on key variables and assumptions? Is it consistent with our internal assessment of strategic direction and long-term value drivers? Have those forward-looking statements, and any explanatory text that accompanies them, been subject to legal review? | ■ | ■ | ■ | ■ |
| How should our disclosures evolve in response to recent developments in regulatory, institutional and shareholder expectations, and relevant litigation? | ■ | | ■ | ■ |
| Do we make any other 'voluntary' disclosures in relation to climate change-related risks – including (for example) a separate sustainability report or response to CDP (formerly the Carbon Disclosure Project) questionnaire? If so, how does management ensure that statements in our annual reports and continuous disclosures are consistent with any voluntary disclosures? What steps have been taken in consultation with external auditors to address the challenges of assurance over these forms of emerging forms of external reporting? | ■ | | ■ | |
| On the basis of the above, are we satisfied that there are reasonable grounds to base our view that all potential material climate-related risks to our performance and prospects have either been appropriately disclosed, or resolved as not material? | ■ | ■ | ■ | ■ |

# Your MinterEllison contacts

## MELBOURNE

**Sarah Barker** Special Counsel
**T** +61 3 8608 2928 | **M** +61 402 220 556

**David Eterovic** Partner
**T** +61 3 8608 2420 | **M** +61 412 228 303

## SYDNEY

**Maged Girgis** Partner
**T** +61 2 9921 4410 | **M** +61 419 886 662

**Keith Rovers** Partner
**T** +61 2 9921 4681 | **M** +61 411 275 823

## BRISBANE

**Brendan Clark** Partner
**T** +61 7 3119 6455 | **M** +61 421 617 096

**Simon Scott** Partner
**T** +61 7 3119 6153 | **M** +61 401 101 215

## PERTH

**Mikes Hales** Partner
**T** +61 8 6189 7825 | **M** +61 411 343 313

## NEW ZEALAND

**Lloyd Kavanagh** Partner
**T** +64 9 353 9976 | **M** +64 21 786 172

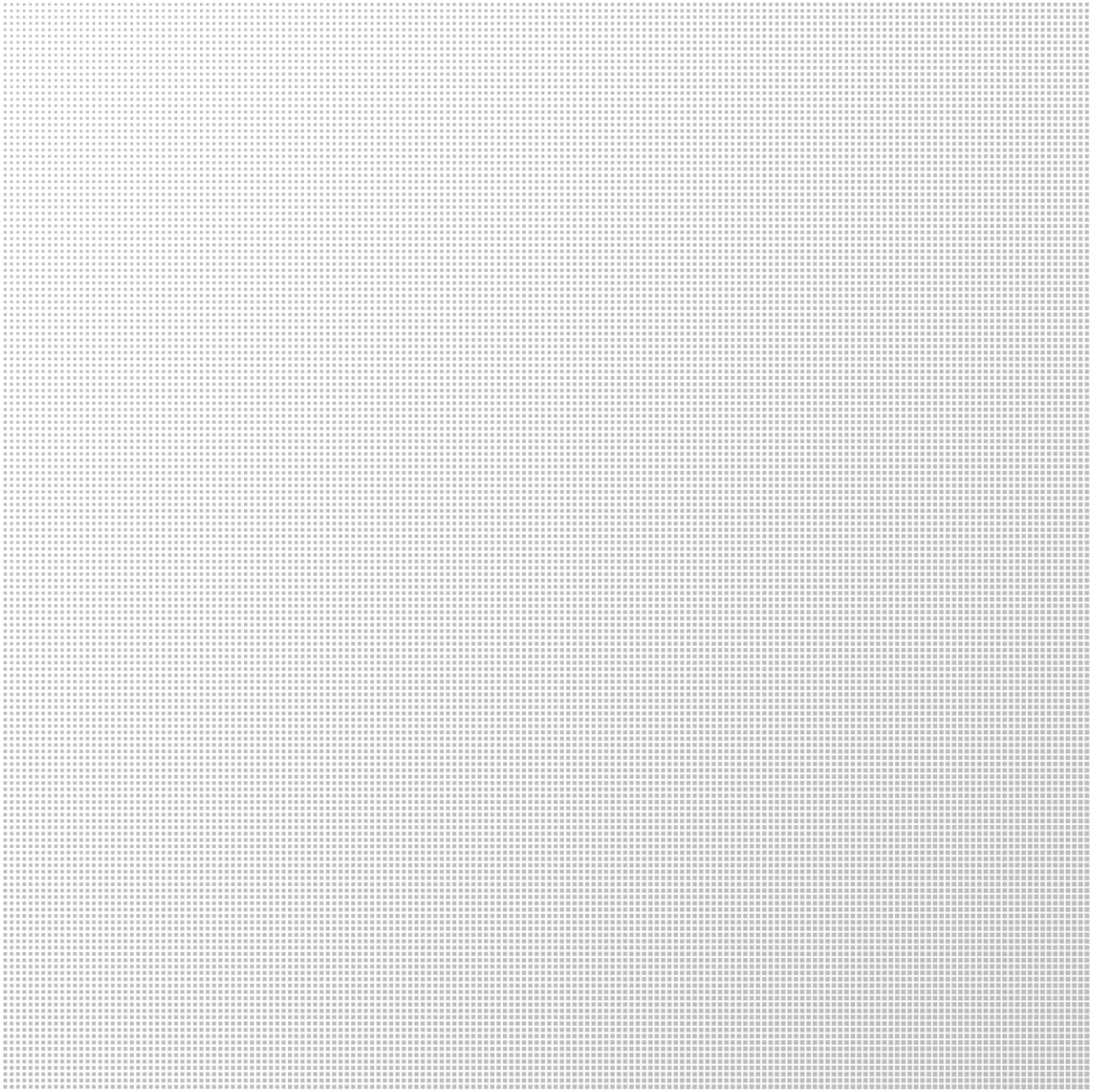
EMAIL: firstname.lastname@minterellison.com



CPD CENTRE FOR POLICY DEVELOPMENT 10TH ANNIVERSARY

COMMONWEALTH Climate and Law Initiative

MinterEllison





CENTRE FOR POLICY DEVELOPMENT
10TH ANNIVERSARY

COMMONWEALTH Climate and Law Initiative

MinterEllison