



## ENHANCING BANKS' AND INSURERS' APPROACHES TO MANAGING THE FINANCIAL RISKS FROM CLIMATE CHANGE

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ICAEW welcomes the opportunity to comment on the consultation paper *Enhancing banks' and insurers' approaches to managing the financial risks from climate change* published by the Prudential Regulation Authority on 15 October 2018, a copy of which is available from this [link](#).

ICAEW agrees that the PRA and other regulatory bodies are well placed to encourage banks and insurers to mitigate the financial risks from climate change and would be pleased to assist with the efforts. We agree that an effective but proportionate strategic approach will have to be followed by firms to be able to address and oversee the risks arising from the unique challenges.

The approach outlined in the consultation paper is an important step in achieving consistent best practice in the marketplace. We however recommend that when building measurement and monitoring of climate change related efforts into the existing supervisory framework regulated firms must be made aware of the criteria which they are assessed against. It is also critical that a timeframe is established around the regulatory expectations.

This response of 15 January 2019 has been prepared by the ICAEW Financial Services Faculty. As a leading centre for thought leadership on financial services, the Faculty brings together different interests and is responsible for representations on behalf of ICAEW on governance, regulation, risk management, auditing and reporting issues facing the financial services sector. The Faculty draws on the expertise of its members and more than 25,000 ICAEW members involved in financial services.

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## KEY POINTS

1. ICAEW welcomes the opportunity to comment on the Prudential Regulation Authority's (PRA) consultation on *Enhancing banks' and insurers' approaches to managing the financial risks from climate change*, published in October 2018.
2. The PRA and other financial regulators are well positioned to take a strategic view of the risks arising from climate change and to incorporate the risks explicitly into their governance, risk management frameworks and disclosures.
3. The principles outlined in the consultation paper represent an important step in the process of bringing the issues front and centre and convince firms of the regulators' determination of converging good practice and importantly, support and give guidance in achieving it.
4. ICAEW particularly supports extended alignment of disclosures related to financial risks from climate change. Increased, consistent disclosure will support transparency and allow necessary data to be obtained for risk assessment and development of risk mitigation methodologies. Regulatory support for adoption of the recommendations of the Task Force for Climate-Related Financial Disclosures (TCFD) is welcome.
5. ICAEW would be pleased to assist the PRA with the efforts to raise awareness and understanding as well as finding practical ways to achieve more consistent approaches to climate change risk management.

## DETAILED COMMENTS ON THE APPROACH OUTLINED IN THE PAPER

### Strategic approach

6. We agree that an effective but proportionate strategic approach will have to be followed by firms to be able to address and oversee the financial risks arising from climate change. To be able to consider a sufficiently long-term view, governance, risk management, scenario analysis and disclosure will have to bear equal weight.
7. Addressing financial risks from climate change through existing risk management frameworks makes it more likely that the process becomes part of "business as usual" more rapidly.
8. We agree with the PRA's assessment of the distinctive elements of the financial risks from climate change and the fact that they present a unique challenge requiring a strategic approach.
9. The expectation that firms' approaches to climate change will mature over time should empower firms to experiment and try different ways of assessing the associated risks. To date, many banks (for example) that are currently working on a response to recommendations of the Taskforce on Climate-Related Financial Disclosure (TCFD) are focused on credit risks with less attention on market and operational risks. Consequently, we believe that introducing a realistic timeframe around the PRA's expectations would help firms focus and concentrate their efforts.

### Supervision

10. Building measurement and monitoring of climate change related efforts and achievements into the existing supervisory framework is a laudable aim and would doubtless go some way achieving the regulator's target.
11. However, supervised firms must be made aware of the supervisory parameters and know how their accomplishments are measured and what the monitoring criteria are. Publishing an assessment of the progress some time into the future would also enable regulated firms to evaluate their own progress against peers and competitors.
12. Any guidelines provided should include illustrative examples of metrics and targets. While overarching principles of policy are possibly acceptable for all sectors, detailed targets should be set on a sector by sector basis. This should go some way in clarifying what the

regulator expects as well as reducing diversity in disclosures. It would also acknowledge the need for flexibility to reflect the very varied challenges that particular sectors face. A uniform approach is unlikely to be effective or gain widespread acceptance.

13. Further guidance on how to calculate key metrics would be useful and could also encompass scenario analysis disclosures. This would promote the usefulness of the disclosures in terms of comparability. It would also assist organisations preparing climate-related financial disclosures for the first time, while not discouraging other organisations from experimenting with disclosures and metrics outside of the key metrics prescribed.
14. It will be important to set expectations clearly, emphasising the need to avoid complexity and clarifying that it will be acceptable for organisations to build up disclosures and scenario analysis over time rather than implement changes rapidly or completely. The activities of larger firms within financial services, for example, are more likely to directly impacted by climate change. We therefore believe that disclosures should be proportionate to the size of the reporting entity and the expected impact of climate change on its business model and the sector it operates in.
15. ICAEW's stakeholders often mention the unavailability of appropriate data. This is a valid concern, but not an enduring excuse for lack of sufficient efforts. The PRA could outline alternative ways of presenting information. A range of qualitative and quantitative tools and metrics to substitute the missing data would allow regulated firms to make a meaningful start even if they are unable to obtain data of suitable quality.
16. The paper clearly states that the PRA will expect firms to evidence how they will mitigate financial risks from climate change. This is essential to be able to hold firms to account. Some guidance on the form of acceptable ways of evidencing would be helpful for firms to make progress.
17. The PRA expect all firms to engage with wider initiatives on climate-related financial disclosures and to take into account the benefits of disclosures which are comparable across firms. A widely publicised and freely available knowledge hub would help firms engage with the numerous initiatives in a meaningful way. This would need to be set up, monitored and administered.

## Scenario Analysis

18. We support the recommendation for scenario analysis and disclosure of the results. We agree that it will be useful for informing strategic decisions, stimulating discussion at board level. Initially scenario analysis should inform strategy and business models qualitatively. Detailed, descriptive scenario analysis would be of limited use.
19. However, producing such disclosures will be challenging for many companies, especially those with little experience of disclosing climate-related issues. Certainly in the work that ICAEW has conducted recently on scenario analysis, this has been a common refrain.
20. As discussed above, experimentation will be an important factor in ensuring that this recommendation is successfully adopted by organisations. This approach will allow larger companies, with the necessary resources available, to lead by example and allow smaller companies which may wish to undertake such analysis to benefit from their experience.

## Disclosure

21. ICAEW agrees with the expectations set out by the PRA. The key initiative for improving climate-related disclosures is the adoption of the recommendations of the TCFD, and its incremental implementation in the agreed timetable.
22. To date there has been multiple sustainability reporting standards. Global harmonisation of the disclosures is important for firms, particularly large, international institutions. We would note, however, that standardisation of reporting standards should not result in prescriptive frameworks, as climate change-related risks will continue to evolve over time. ICAEW prefers principle-based reporting frameworks, which allow for companies to disclose their response to the most material issues.

## External Assurance

23. The approach outlined in the consultation paper makes no reference to the need for assurance. Our view is that some disclosures and the processes that underpin them will lend themselves to external assurance.
24. Over the coming years finance professionals will play an increasingly important role in measuring and verifying a company's transition to a low-carbon economy, as well as increasing external disclosure to meet the needs of capital markets and society. This topic would benefit from further consideration in due course.