Future First℠ Insights

Tackling the TCFD Challenge: Issuer Considerations and Investor Preferences in Disclosure

BNY MELLON
Consider Everything

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About the TCFD

The Task Force on Climate-Related Financial Disclosures (TCFD) was established to develop recommendations for more effective climate-related disclosures that could promote more informed investment, credit and insurance underwriting decisions.[1] It was intended that these disclosures would, in turn, enable other stakeholders to better understand the concentration of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks. Furthermore, the framework was created to assist companies in incorporating climate-related risks and opportunities into their risk-management and strategic-planning processes.

In 2017, the TCFD issued 11 voluntary recommendations known as the TCFD Framework.[2] These recommendations cover four core elements—governance, strategy, risk management, and metrics and targets.[3]

Figure 1: *The Four Core Elements of the TCFD*

Governance – The organization's governance around climate-related risks and opportunities

Strategy – The actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy and financial planning

Risk Management – The processes used by the organization to identify, assess and manage climate-related risks

Metrics and Targets – The metrics and targets used to assess and manage relevant climate-related risks and opportunities

Report Summary

The four core elements identified by the TCFD *(see Figure 1)* cover two distinct areas – the preparation for disclosure and the subsequent disclosure itself. Each of these have important implications beyond sustainability teams both for leaders in a company's C-suite and for their investor relations teams.

The preparatory stage is intended to lead companies to analyze their overall governance, strategy and the underlying climate-related risks in their operations. This systematic approach to the TCFD Framework, including analyzing specific metrics and targets, enables companies to make decisions about how to allocate resources in ways that incorporate climate-related risks and opportunities into their planning processes. The analysis of risk and benefits in the company's sustainability strategy involves coordination among sustainability teams and all the departments that manage ESG-related risks. In turn, disclosure of that analysis requires coordinated effort across sustainability teams, legal, corporate governance and investor relations, as well as C-level approval.

The second stage, adding regular disclosure on climate risk, addresses the needs of investors and society more broadly for sustainability information. Companies intend for this disclosure process to provide meaningful data and information about their governance, strategy, risks and performance to investors to aid in their decision-making.

As a company moves forward with TCFD implementation, it may need to overcome common hurdles, such as additional costs that may be incurred, challenges in obtaining senior management buy-in, assignment of ownership of responsibilities and a lack of consistent data available within the organization. BNY Mellon researched the current recommendations on best practices for climate disclosure and interviewed a range of issuers and investors, in order to support companies as they plan to disclose their climate-change policies, strategy and data. We recommend the following systematic approach to implementing the TCFD Framework:

1. **Lay a foundation**
2. **Identify and prioritize key climate-related risks and opportunities**
3. **Assess financial impacts through scenario analysis**
4. **Develop and implement a risk-informed climate strategy**
5. **Communicate effectively**

Each of these steps are described below in greater detail under the section "The Steps to Implementation" (page 12).

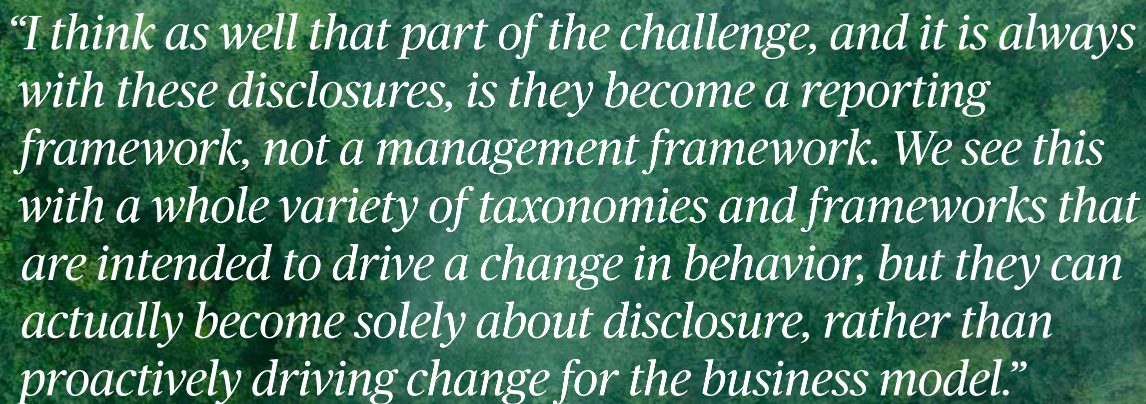
The Case for Adoption

Companies across industries and geographies have increasingly added sustainability to their C-suite agendas in recent years, as stakeholders including investors, employees, regulators and customers have highlighted it as a priority. As these issues have gained importance, the merits of adopting the TCFD guidelines have become more evident, with the overall rationale for doing so resting primarily on three drivers:

- the **business case** and its strategic, financial and operational impacts
- **investor demand** for information
- the trend of **increasing regulatory mandates** requiring its adoption.

The benefits from both a well-prepared and then well-executed sustainability disclosure program provide a strong case for comprehensively implementing the TCFD guidelines.

Business case: The business case for TCFD reporting is rooted in the understanding that effective, business-aligned sustainability practices can contribute to better bottom-line performance for companies. Extensive research[4] has found a strong positive correlation between financial performance and sustainability performance, with one recent study indicating that the net present value realized over a five-year period from superior sustainability practices can be as high as 12% of annual revenue.[5] TCFD reporting can contribute to sustainability outperformance, as the process requires a detailed and thoughtful evaluation of sustainability and climate-related risks to the business model. Discovery of these risks is helpful to management in uncovering potential issues and identifying possible solutions to these challenges.



"I think as well that part of the challenge, and it is always with these disclosures, is they become a reporting framework, not a management framework. We see this with a whole variety of taxonomies and frameworks that are intended to drive a change in behavior, but they can actually become solely about disclosure, rather than proactively driving change for the business model."

—**Kristina Church,** *Head of Responsible Strategy, BNY Mellon Investment Management*

"Companies should be aware that as a supplier, you can lose business if you're not providing adequate disclosure, because we're seeing, in an effort to improve their own disclosure and management of risks, companies are reaching further and further into the supply chain, particularly to more comprehensively disclose Scope 3 greenhouse gas emissions."

—**Maria Lernerman,** *ESG and Global Consumer Research Analyst, Harding Loevner, LP*

Investor demand: The business imperative for companies to implement TCFD-aligned disclosure is buttressed by investor demand for these disclosures. The PRI[6] reports that the largest investor groups in the world, representing over US$103 trillion in assets under management, have urged that corporate reporting appropriately reflect climate-related risks.[7]

> *"If you look at the progression and the asset growth of Responsible Investment/ ESG, it's clearly both significant and a long-term trend. You don't want to be an issuer who's not providing appropriate disclosures, with investors then potentially looking elsewhere."*
>
> ***—Frederick Isleib,*** *Director ESG Research and Integration, Manulife Investment Management*

Other investor-centric initiatives have begun to emerge creating more urgency for companies to disclose under the TCFD Framework, including:

a. **PRI signatories are now required to disclose some metrics according to the TCFD recommendations –** In 2019, the PRI announced that signatories would be required to report certain climate indicators in accordance with TCFD-aligned practice.[8] Given this requirement, it is logical that investors would expect their investee companies to disclose under the same framework, making signatories' reporting obligations more manageable.

b. **Industry initiatives requiring investor TCFD reporting have emerged –** For example, the Net Zero Asset Managers Initiative, launched in December 2020, is a commitment by asset managers to support investing aligned with net zero emissions by 2050 or sooner. Signatories are required to publish TCFD disclosures that signal alignment with the commitment, and, as such, will need companies to disclose TCFD-aligned information so that they are able to confirm this commitment.[9, 10]

c. **Large investor coalitions are encouraging adoption –** Coalitions such as Climate Action 100+, Ceres Investor Network and the Investor Leadership Network are encouraging companies to embrace and implement TCFD-aligned reporting.[11]

"If I'm an issuer in an industry that's carbon-intensive and my numbers are better than my competitors' for one reason or another, why wouldn't I want to highlight that aspect?"

—Frederick Isleib, *Director ESG Research and Integration, Manulife Investment Management*

Increasing regulatory mandates: The fact that mandatory reporting is gaining traction is further rationale for companies to adopt the TCFD guidelines. While at present, TCFD reporting is generally voluntary for listed companies, several government regulators have either approved new regulation or announced their intention to enact regulation that will mandate TCFD reporting in their respective jurisdictions, including Australia, Brazil, Canada, the European Union, France, Japan, New Zealand and the United Kingdom.[12] It is likely the trend of mandating TCFD reporting will continue, and companies would benefit from getting ahead of the curve to position themselves as market leaders, and also enjoy the benefit of implementing the reporting at a measured, comfortable pace.

Some companies have questioned whether adoption is necessary, particularly those not closely tied to environmentally sensitive industries. However, all industries are affected to some degree by climate change, making the case that all companies from all industries should provide TCFD-aligned disclosures relative to the impacts specific to their business model. Both the immediate internal and investor benefits as well as the aforementioned rising tide of initiatives make a firm case for adoption. As a result of these pressures, the pace of adoption could begin to accelerate.

The Pace of Adoption

As previously noted, one of the primary aims of creating the TCFD Framework was to provide climate-related disclosures to allow more informed investment, credit and insurance underwriting decisions. For this to occur, however, sufficient uptake by companies will be necessary in order for investors to access enough data to make educated, comparative assessments on the prospects of a company. Accordingly, it is imperative to monitor companies' pace of adoption of the TCFD Framework to understand how widespread its usage is, given higher level of adoptions can potentially influence policy decisions with regards to mandating disclosure based on the TCFD Framework.

But monitoring the pace of adoption is not easy, as there is no centralized repository that collects and aggregates TCFD reporting across all industries and geographies. Instead, the TCFD estimates adoption by conducting an annual assessment of a sample of companies (1,651 in 2021) in eight industries,[13] using an AI-based approach that automatically identifies TCFD-aligned disclosures in financial filings and other company reports. While this method provides a representative indication of disclosure rates, it also results in gaps in information for industries outside of the scope of the review.

The result of this review is published annually in the TCFD Status Report. The latest edition, released in October 2021, estimates that 50% of companies are disclosing in alignment with at least three TCFD recommendations. That number increases to 75% when considering companies that are disclosing in alignment with at least one recommendation.[14]

Other information included in the latest analysis, based on 2020 reporting, includes[15]:

- **Implementation of disclosure on Risk & Opportunities (a sub-element of Strategy) was the highest,** with 52% of companies making disclosures.
- **Resilience of Strategy** (a second sub-element of Strategy that replaces "Scenario Analysis" from the TCFD's 2019 Status Report[16]) **has the lowest implementation rate, with just 13% of companies reporting this information.** This low rate of adoption may stem from the many challenges to creating a robust and reliable scenario analysis.
- **The higher the market cap, the higher the rate of disclosure.** Large-cap companies (>$12.2 B) disclosed information at the highest rates, with an average disclosure rate of 44% across the 11 recommendations. Mid-cap companies ($3.4 B - $12.2 B) and small-cap companies (< $3.4B) had average disclosure rates of 31% and 20%, respectively.
- **In Europe, 50% of companies have implemented disclosure** according to the recommendations, far ahead of companies in Asia-Pacific (34%), Latin America (26%), Middle East & Africa (22%) and North America (20%).
- **Industries more closely linked or exposed to climate change reported at higher rates.** Materials and Buildings and Energy companies had the highest submission rates across the recommendations, at 38% and 36%, respectively. Technology & Media (16%) registered the lowest average, a full 10 percentage points below Consumer Goods and Transportation at 26%.

“We believe those gaps (in TCFD disclosure) are inhibiting the market mechanisms to accurately price in climate risks and opportunities.”

—Frederick Isleib, *Director ESG Research and Integration, Manulife Investment Management*

A review of the results from the 2021 Status Report provides a level of optimism, as disclosure in one of the recommendations (Risks & Opportunities) surpassed 50% for the first time, demonstrating growth in adoption. As well, with 75% of the companies reviewed in the latest Status Report disclosing against at least one recommendation, and 50% reporting against three of the recommendations, we can see that the TCFD Framework is starting to resonate with more companies. But the fact remains that very few companies are currently reporting against all, or even a majority of the recommendations, which makes it difficult for investors to fully incorporate climate-related data into their investment process. However, from a big-picture perspective, it is important to recognize that it is also still early days. The Task Force estimated when they released the recommendations that full implementation for most adopting companies would take five years. Subsequently, for early adopters, resulting full disclosure will not occur until 2022, which demonstrates the long trajectory for a significant volume of data. Still, even with this caveat, the Task Force has acknowledged the need for more adoption. Participants in our interviews (see “Investor Perspectives on Disclosure,” page 24) said they expect that the Task Force is likely to address standards and comparability issues, as more companies adopt the TCFD Framework or expand the scope of the recommendations for which they are currently providing information. This should help drive adoption rates upward.

The Steps to Implementation

We expect an increasing number of companies to report TCFD-aligned disclosure. With the support of input from S&Z – Consultants for Corporate Responsibility, an international management consultancy specializing in corporate responsibility and sustainability, we have identified five critical steps that a company should take once leadership makes the decision to implement such disclosure.

1. Lay the foundation

- Summarize the motivation and business case for engaging with climate risk, outlining the high-level benefits of TCFD reporting.
- Budget and plan for the collection and reporting of additional data, new software systems and data management protocols.
- Recruit a cross-functional management team, including members from sustainability, strategy, risk management, operations, finance and supply chain and possibly corporate functions and business unit or regional market heads.
- At the first management team meeting, review the company's climate-related activity to date, clarify expectations and assign clear roles.

"Governance is the route to good risk management and where a lot of companies often fail is because they don't have the right governance to take climate risks seriously."

—***Kristina Church,*** *Head of Responsible Strategy, BNY Mellon Investment Management*

2. Identify and prioritize key climate-related risks and opportunities

- Narrow the scope of the analysis to risks and opportunities relevant to the company. Typical criteria to prioritize are the likelihood, scope and scale of impact. A best practice is to subdivide categories—for example into acute risks, such as storms, or chronic risks, such as recurring heat waves—using TCFD guidance documents,[17] relevant literature, expert surveys, trend analyses and historical data.
- Assess the resilience of the company and its ability to respond to the respective risk or opportunity.

3. Assess financial impacts through scenario analysis

- Conduct scenario analysis to explore multiple plausible future consequences of climate risks and opportunities for the company and to suggest appropriate and necessary responses.
- Define the scope of scenario analysis and precise methodology. For example, some companies may choose to follow a granular, asset-based approach, while others may prefer a broader country-level approach.
- Develop and test at least two scenarios, including one where global temperature increase is limited to well below 2°C (in alignment with the Paris Agreement).[18] Scenario results can be quantitative or qualitative. Results help identify the risks and opportunities most relevant to the company and identify the associated impacts on its business and can subsequently be utilized to inform and update strategy.

Just 13% of companies reviewed by the TCFD have conducted and published scenario analysis aligned with this recommendation.[19] Given that scenario analysis is amongst the more challenging and complex of the disclosures, we expect comprehensive reporting under this recommendation to most likely occur toward the end of the suggested five-year TCFD implementation period. This held true in the interviews we conducted for this study and in our discussions with issuers on this topic.

The TCFD recommends that companies "start with qualitative scenario narratives or storylines to help management explore the potential range of climate change implications for the organization." Once these are established, companies can use quantitative information to illustrate potential pathways and outcomes.[20]

4. Develop and implement a risk-informed climate strategy

- Identify climate-related risks over the short, medium and long term.
- Leverage scenario analysis findings to strengthen business strategy, risk management and approach to ESG.
- Translate the findings into clear goals and action plans, with measures of success, that can improve the company's resilience.
- Assess implementation through periodic monitoring of progress, including at minimum an annual data collection.
- Develop a governance and management structure to oversee the work and report to the C-suite and board of directors.

5. Communicate effectively

- Provide insights into governance and risk management related to climate risk when reporting a company's financial and operational performance.
- Follow any requirements that are mandated by your specific national legislation or other regulatory bodies.
- As best practice, make TCFD disclosure information available and accessible, no matter where it is ultimately published.

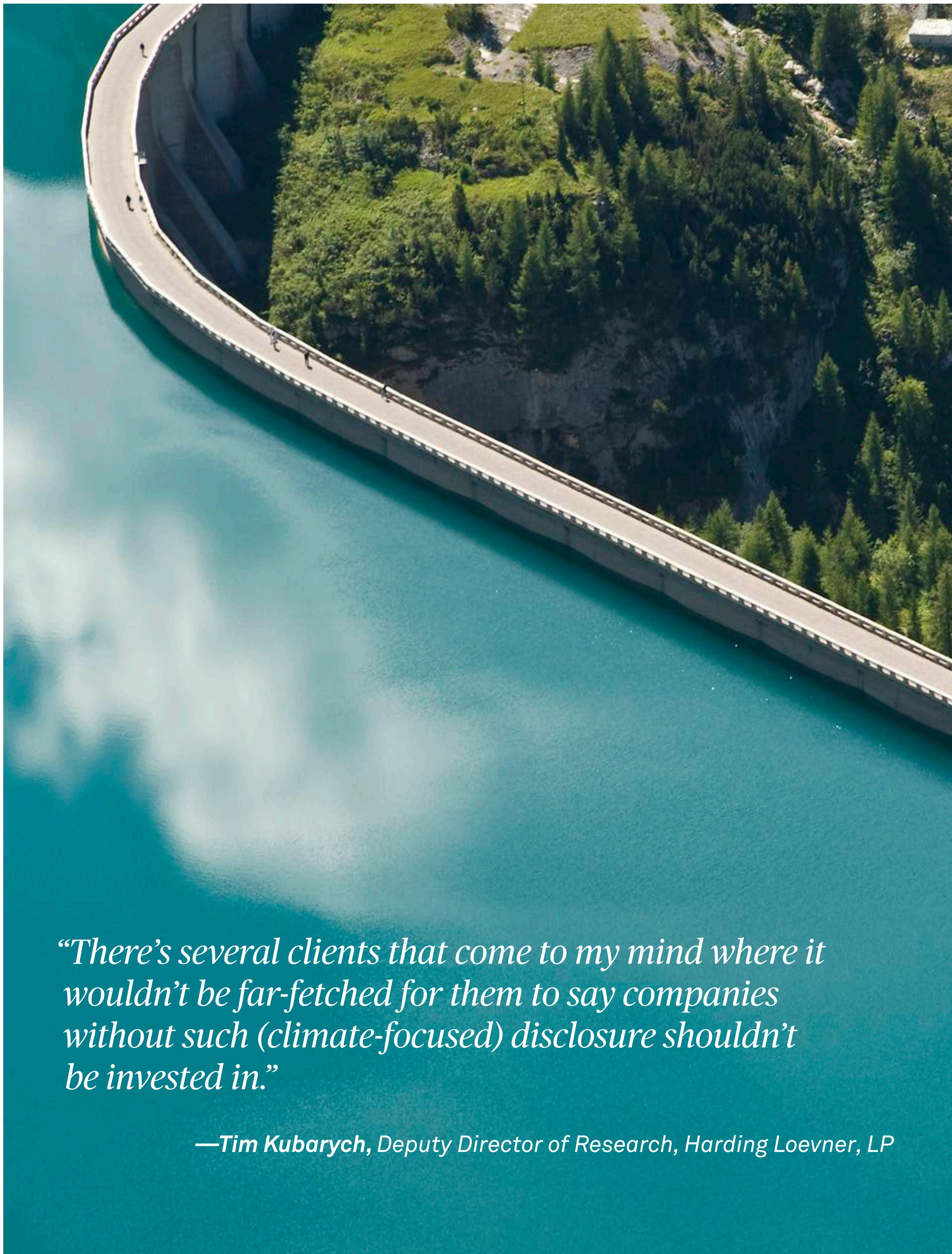
Where to disclose

A variety of factors influence where to disclose information, including requirements mandated by specific national legislation or regulation. We recommend that the information be prominently displayed on a company's website, accompanied by a press release promoting the inclusion of TCFD information in the document.

TCFD disclosure is typically found in the following company publications:

- **Annual Report:** The TCFD recommends that such information should be included in a company's annual report, as a primary public document. However, gaining space in what may be an already crowded and voluminous document can be a challenge.
- **Sustainability Report:** Many companies are now publishing a dedicated ESG report and consider this report as the natural landing spot for TCFD disclosure. In some cases, companies dedicate a section of their sustainability report specifically to TCFD reporting.
- **Dedicated TCFD Report:** A dedicated report generally follows the format and order of the TCFD recommendations, making it easy for stakeholders and investors to locate specific disclosures.

Regardless of where TCFD information is disclosed, if this information (or any sustainability disclosure), appears across multiple documents/platforms, all documents must be consistent. This is imperative not only from a reputational perspective, but also due to liability and financial considerations, as regulators intend to give much scrutiny to sustainability information.[21]



"There's several clients that come to my mind where it wouldn't be far-fetched for them to say companies without such (climate-focused) disclosure shouldn't be invested in."

—Tim Kubarych, *Deputy Director of Research, Harding Loevner, LP*

Hurdles and Challenges to Adoption

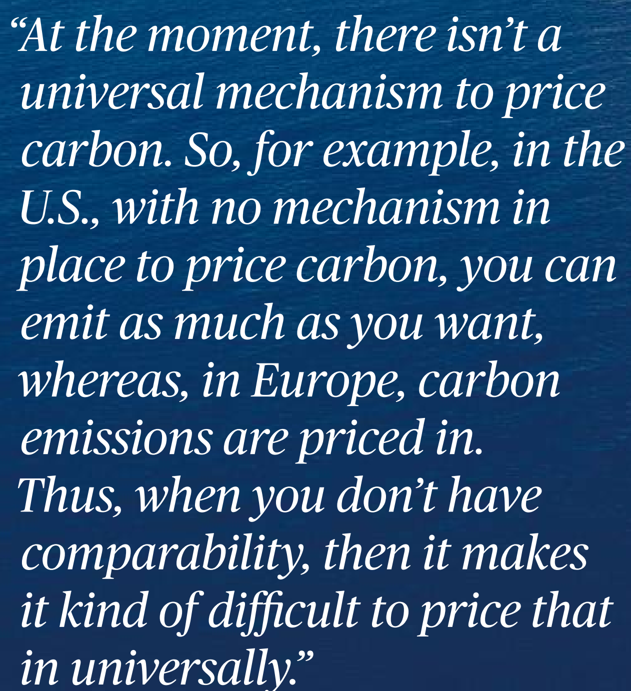
Although the rationale for adopting the TCFD Framework is clear, the path can be challenging. Companies often experience similar challenges, outlined below, as they prepare for and implement disclosure. Beginning with Step 1, laying the foundation, companies should address and implement methods to address these challenges.

Additional cost and resources: Companies that have not collected climate-related data in the past may face significant new costs in beginning to do so: additional headcount to manage the disclosure project, software for data collection and consultants to guide the process. One issuer we interviewed estimated that upfront cost to implement TCFD-aligned disclosure would total $700,000 to $800,000 during the first year.

Senior management and board commitment: The mandate for climate-related disclosure, as an integral element of a company's overall business strategy, must come from the top. Members of senior management and the board may have varying degrees of education and experience on the impact of climate risks on the company's business operations. As a result, senior buy-in for TCFD-aligned disclosure may require additional lead time, particularly for companies in sectors not traditionally considered climate-sensitive. Furthermore, some management members may not be comfortable disclosing negative climate-related data. During our interviews, one company revealed the timeline for CEO buy-in to proceed with TCFD-aligned disclosure was more than two years from the time the CEO was initially approached for approval.

Ability to quantify benefits: Some of the advantages of TCFD-aligned disclosure are considered intangible benefits, such as corporate reputation or investor good will. These benefits may take time to emerge and pose challenges to quantify. Reputation and goodwill are also difficult to define, model mathematically, and measure and report, making it more difficult to demonstrate a compelling rationale to senior decision makers.

Gaps in the current data available: Some of the required data may either be unavailable, inconsistent and/or complicated to access. This particularly applies to the TCFD recommendation "Resilience of Strategy." Although standards and tools are emerging, lack of accurate and consistent data poses challenges when projecting different scenarios and pursuing implications. As the TCFD points out, the main challenge of estimating actual financial impact is effective attribution to climate-related events, since financial effects may have multiple drivers beyond climate.[22]



"At the moment, there isn't a universal mechanism to price carbon. So, for example, in the U.S., with no mechanism in place to price carbon, you can emit as much as you want, whereas, in Europe, carbon emissions are priced in. Thus, when you don't have comparability, then it makes it kind of difficult to price that in universally."

—Frederick Isleib,
Director ESG Research and Integration,
Manulife Investment Management

With a disciplined approach, informed by the experiences of companies that have already made progress, adopters of the TCFD Framework can realize benefits for the business that will be welcomed by capital markets, customers and other stakeholders.

- The TCFD was established to fill a void in understanding the risks and opportunities related to climate impact on companies.
- Companies reap benefits both from disclosure itself and from processes required to implement such disclosure.
- Preparing to implement the TCFD Framework helps companies identify gaps in strategy and risk management.
- Disclosing under the TCFD Framework allows companies to appeal to investor needs for better material data and to adapt to broader societal trends.
- Providing TCFD-aligned disclosure can assist in improving sustainability practices, which, according to research, often correlates with improved financial performance.
- Companies must overcome challenges to prepare for and implement the TCFD Framework, including additional costs, management buy-in and inconsistent data.

“The planet is on red alert, and if you’re not doing a TCFD report and understanding and reporting your risks, you’re certainly doing yourself a disservice, your customers a disservice, your shareholders a disservice, and probably the planet a disservice.”

—Kristina Church, *Head of Responsible Strategy, BNY Mellon Investment Management*

Overall, the disclosure process can unlock highly valuable intelligence about a company’s strategies, risks and long-term potential for value creation, as illustrated by the case studies and investor perspectives on the following pages. The process equips boards and executive teams with a vital source of insight. Comprehensive disclosure under the TCFD Framework also sends a signal to markets that companies are proactively evaluating all risks and opportunities and positioning themselves as sustainable for investors. As such, it becomes an important tool in the Investor Relations toolbox, with the ability to answer and even anticipate investors’ questions about the holdings in their portfolios.

Case Study

Itaú Unibanco: *Ahead of the Curve with Early TCFD Adoption*

As of the end of 2020, Itaú had implemented 79% of the TCFD recommendations and anticipates reporting against all recommendations by 2022.

Fabio Luiz Guido, Climate Risk Team Leader at Itaú, credits the firm's early decision to implement the TCFD reporting Framework as "a very useful instrument for Itaú's internal analysis. Its use allows Itaú to be comparable to other banks in the world."[23] The company's partnerships with organizations like the UNEP FI[24] and the Brazilian Federation of Banks have provided guidance, enabling the company to implement TCFD reporting swiftly and emerge as a first mover and leader within Brazil.

Benefits: The TCFD reporting Framework complements that of Itaú, whose climate finance efforts are assigned to a squad led by the Climate Risk unit, focused on managing risk, and the sustainability area, dedicated to exploring opportunities and defining strategies. The firm's structure aligns with the TCFD Framework's twin goals of providing disclosure on a company's recognition of the risks and opportunities created by climate change.

Guido expects Itaú's first mover standing to serve it well, especially when pending Brazilian Central Bank regulation makes climate risk management and disclosure mandatory. Labes commented that "TCFD helped us to be prepared for what was coming. Institutions that are starting now will have more challenges and a more compressed timeline to adhere to the disclosure mandates."

Challenges: Guido cited the lack of standard methodologies for some recommended data disclosures. For example, the TCFD's recommended disclosure of Scope 3 data, involving emissions which companies measure in different ways, makes comparisons difficult. Supposing Itaú's methodology of measuring Scope 3 emissions is more accurate than a competitor's, that precision may then result in Itaú's reporting higher Scope 3 emissions than the competitor does. Higher reported emissions might lead to unduly harsh risk assessments for Itaú, with knock-on negative effects.

Guido also noted challenges of scenario analysis, such as technical issues in developing the analysis and applying it to Itaú's portfolios. Moreover, incorporating the outputs of the scenario analysis into the firm's decision-making and strategy may require communicating the results to senior executives responsible for setting business strategy, who are sometimes still in the process of more deeply understanding climate risk.

Case Study

BMW: *TCFD Enhances Long-standing Tradition of Sustainability Disclosure*

BMW has been reporting climate-related information since 2001. It is recognized for its commitment and management of climate change by CDP,[25] having earned "Leadership Level" status each year dating back to 2010 in the NGO's annual evaluation of companies.[26] In March 2021, BMW became the first premium automobile manufacturer to publish an integrated report.[27]

BMW was an early public supporter of the TCFD and published its first disclosures in line with the TCFD Framework in its 2019 Sustainable Value Report. Thomas Becker, Vice President of Sustainability and Mobility Strategy, commented, "TCFD allows us to properly integrate sustainability into corporate strategy, reporting, governance and target setting. Additionally, it has allowed us to be well-prepared for what is ahead in terms of more stringent disclosure requirements."

Benefits: The company is strongly committed to driving the electrification agenda, with the TCFD Guidelines playing a role in prompting potential improvements to de-carbonizing its supply chain. Becker noted that "TCFD has assisted monitoring our comprehensive CO2 footprint in a more systematic way. We have developed a transparent tool that evaluates and assists our decision-making by determining the level of CO2 reduction we can achieve based on our spend with the supplier."[28]

The TCFD Framework has helped BMW in effectively managing its climate-focused sustainability process. Becker commented that "the TCFD Framework assists in systematically structuring things, and not having to reinvent the wheel. It provides internal stability and reliability and reduces the workload that otherwise would be going into determining how we should structure and present considerations. Overall, it really adds efficiency to the way we do this."[28]

Challenges: Becker said target setting can be a challenge because a variety of factors are outside BMW's control. For example, in setting emission reduction targets, "it is difficult to predict the speed of the build-up of electric charging infrastructure, which can impact our projections. You have to acknowledge the known unknowns of this system and be as thorough as possible in developing targets and transparently reporting methodology and assumptions. Ultimately, we need to ensure that what we promise we can actually deliver."[28]

Case Study

BNY Mellon: *Adapting the TCFD Framework to Fit a Unique Business Model*

BNY Mellon committed internally to utilize the TCFD Guidelines for reporting in December 2019. After extensive review, a working group decided that the TCFD Framework did not fully align with the structure of BNY Mellon's business. Instead, they decided BNY Mellon's TCFD-aligned reporting will disclose according to each of ten separate business functions, with 27 separate disclosures that adhere to the 11 recommendations.

For example, eight of the ten business functions have disclosure related to Metrics and Targets. According to Amy Springsteel, Director, Enterprise ESG, "metrics and targets should be included throughout because that should be part of the context with which you develop your planning. All of the themes overlap and don't exist in a vacuum separate from the others."[29]

Challenges: There is still a need for greater global coordination amongst regulators. BNY Mellon operates in many markets and complies with different regulations that are incorporating aspects of TCFD into required disclosures. These differing requirements, under different timeframes, place a substantial burden on companies.

Springsteel also highlighted scenario analysis as a challenge. Financial companies, which generally understand the physical risks, may have less experience and knowledge in understanding the transition risks.

Benefits: BNY Mellon's practical approach has been received warmly, based on conversations with investors and stakeholders, who appreciate how the structure has been broken out and also like its transparency and very clear inclusion of climate into its strategy. Forward-looking targets map out a trajectory of expected dates for each of the 27 disclosures on which the company has committed to report.

Springsteel commented that the TCFD has "brought collaborations together that wouldn't otherwise exist, brought employees together and started people thinking about climate change in new ways, particularly with respect to the impacts across differing areas in the bank."[28]

Investor Perspectives on TCFD Disclosure

Interview Participants:

Kristina Church, Head of Responsible Strategy, *BNY Mellon Investment Management*

Frederick Isleib, Director ESG Research and Integration, *Manulife Investment Management*

Tim Kubarych, Deputy Director of Research, *Harding Loevner, LP*

Maria Lernerman, ESG and Global Consumer Research Analyst, *Harding Loevner, LP*

We conducted interviews with select institutional investors to assess, amongst other issues, the impact that TCFD disclosure has had on their investment process and to understand which TCFD-aligned information they value most. We asked them to gauge how successful they believe the roll-out of the TCFD Framework and companies' adoption of its recommendations have been. We also inquired about the obstacles companies are facing that may inhibit implementation of disclosure according to the recommendations.

Across these interviews, we found:

Investors strongly advocate for companies to disclose under the TCFD Framework

The investors we interviewed were all strongly aligned in encouraging companies to disclose under the TCFD Framework because it gives investors the ability to assess climate-related risks and opportunities more accurately. Aside from this central theme, the investors provided other rationales to support company TCFD adoption. Frederick Isleib of Manulife Investment Management cited the growing assets tied to responsible investment and suggested that investors might look elsewhere if issuers do not provide sufficient disclosures. Maria Lernerman of Harding Loevner referenced the fact that many companies, particularly those in emerging markets, are part of the supply chain of global companies that are increasing pressure on their suppliers to provide climate-related disclosure. Specifically, she stated that companies “should be aware that as a supplier, you can lose business if you’re not providing adequate disclosure, because we’re seeing, in an effort to improve their own disclosure and management of risks, companies are reaching further and further into the supply chain, particularly to more comprehensively disclose Scope 3 greenhouse gas emissions.”

Opinions are mixed on whether the TCFD has been effective in its goal of enabling investors to incorporate climate data into their investment process

Overall, investors have a favorable view on the efforts of the TCFD initiative, but its impact on each firm’s investment process has been different. Isleib was the most complimentary, citing Manulife Investment Management’s first foray and continued efforts into evaluating climate risks and opportunities in its portfolio back in 2018. It was assisted in accomplishing this through the UNEP FI pilot program using the Carbon Delta methodology, which is a comprehensive investor guide to scenario-based methods for climate risk assessment in response to the TCFD. Kristina Church of BNY Mellon Investment Management said that the TCFD has “galvanized our affiliated investment firms’ thinking on climate risks and has been helpful for engagement,” but it is also “very top-down, macro-focused, and doesn’t yet factor in enough about the bottom-up risks associated with companies, and therefore, it hasn’t fully captured the ability to drive decision making.”

While TCFD disclosure is a net positive for investors, some struggle with incorporating some of the data into their investment process

Investors cited a lack of standards and comparability as key obstacles to maximizing TCFD disclosure for investment purposes. As an example, Isleib said it can be difficult to compare companies in different jurisdictions, pointing to the lack of uniformity in pricing carbon in the U.S. vs. Europe, for instance. A lack of standards in assessing and reporting Scope 3 emissions was also a key concern for the investors interviewed.

There are no near-term plans to exclude companies that don't provide TCFD-aligned information from investment consideration, but this may be a possibility over the longer term

Investors are primarily concerned with obtaining climate information and do not have rigid requirements regarding how it is delivered. Church remarked that BNY Mellon Investment Management's affiliated investment firms do not require TCFD disclosure for investment, but they increasingly want to know that "companies are compatible with a 2 degree or better world, and that is irrespective of what they report." Isleib noted that Manulife Investment Management is not at the point of excluding companies over TCFD disclosure; however, when it notices "multiple differences between strong disclosure around climate and those that are weaker, this can be a factor in portfolio construction." Additionally, Tim Kubarych of Harding Loevner highlighted that there are specific clients of their firm that would take a lack of climate-related disclosure seriously, and that it "wouldn't be far-fetched for them to say companies without such disclosure shouldn't be invested in." In short, should TCFD disclosure by companies become more commonplace and the market standard, it is conceivable that investors could exclude companies not disclosing according to the TCFD from their investible universe, but for now, that consideration is for the future.

There was no consensus on which TCFD recommendations are the most important

As investment managers have different approaches to investing, it is not surprising that there are individual preferences among them regarding the TCFD-recommended disclosures. Church favored the recommendations related to the governance theme, feeling that "governance is the route to good risk management and where a lot of companies often fail is because they don't have the right governance to take climate risks seriously." Kubarych finds information around the targets used by companies to manage climate-related risks and opportunities to be most important. He believes the metrics and KPIs chosen by a company provide insights into management's incentives and dictate behavior. Isleib leans towards disclosure on strategy, feeling that this is the most direct path to obtaining insights on how a given company is acknowledging and planning around climate-related risks and opportunities.

TCFD disclosure provides investors with insights that go beyond climate-related information

Companies' disclosure provides climate-related information that is valued by investors, but in addition to this very important function, all the investors were emphatic that TCFD disclosure, or lack of it, also provides them with more subtle clues about a company. For example, Lernerman commented that TCFD disclosure provides "a glimpse into the culture and the running of the company in a way that financial reporting does not." Kubarych stressed that "if companies feel that they are an exceptional, differentiated business, they should be willing to be transparent and provide information to the public. On the other hand, if companies believe that their competitive advantage is being secretive and not being honest about the potential risks to your business, then that doesn't sound like a sustainable business to me." Church linked a company's provision of TCFD-aligned information to their credibility, stating that "the planet is on red alert, and if you're not doing a TCFD report and understanding and reporting your risks, you're certainly doing yourself a disservice, your customers a disservice, your shareholders a disservice, and probably the planet a disservice."

About this Report

BNY Mellon has developed this report as a resource to support companies that have started to publicly disclose their policies, strategy and data regarding climate change, as well as those that have yet to commit to disclosing on climate-related financial issues as part of their overall sustainability strategy.

In preparing this study, we conducted research on the current recommendations on best practices for climate disclosure prepared by the Task Force on Climate-Related Financial Disclosures (TCFD). We also interviewed a range of issuers and investors to elicit their views on climate change disclosure. We then developed a macro-overview of the steps needed to implement disclosure under the TCFD Framework, with the support of input from S&Z - Consultants for Corporate Responsibility, an international management consultancy.

BNY Mellon's Global Investor Relations Advisory Team includes direct experience in Investor Relations, Proxy Solicitation, Equity Capital Markets, Equity Sales Support and much more. Our diverse backgrounds complement our research and analysis of our extensive data sets, including best practices in Investor Relations.

This document does not constitute legal advice and does not purport to offer or provide guidance as to market reporting requirements applicable to climate-related matters for any specific company. Companies must seek the advice of legal counsel regarding climate-related disclosure obligations.

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