ClientEarth

October 2024

CP24/12: Consultation on the new Public Offers and Admission to Trading Regulations regime

ClientEarth response

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Background

ClientEarth is an international non-profit environmental law organisation headquartered in London. Our Accountable Finance team focuses on the legal implications of climate change and other environmental issues for a wide spectrum of market participants, including banks, companies, investors, directors, professional advisers, stock exchanges and regulators.

This document responds to FCA consultation paper *CP24/12: Consultation on the new Public Offers and Admission to Trading Regulations regime (**POATRs**)*.[1] We welcome the opportunity to provide our views on the FCA's proposals and to continue our engagement with the FCA regarding specific requirements for 'mineral companies'. We also thank the FCA for acknowledging our previous submissions in paragraph 6.46 of CP24/12, and opening this crucial topic up to broader input via the consultation.

We welcome further discussion with the FCA on any of the topics below. For any follow up questions, please contact Robert Clarke (rclarke@clientearth.org), Catriona Glascott (cglascott@clientearth.org) and Megan Clay (mclay@clientearth.org).

[1] CP24/12: Consultation on the new Public Offers and Admission to Trading Regulations regime (POATRs) | FCA.

Sustainability-related disclosures in prospectuses for admission to trading on a regulated market

Question 31: Do you agree with the proposed climate disclosure rule to prompt relevant and financially material information to be included in prospectuses? Y/N. Please give your reasons. If not, what should be done differently?

Yes – we broadly support the FCA's proposals to require enhanced sustainability-related disclosures at the point of listing, subject to the comments below.

We repeat the submissions made in pages 2 to 9 of ClientEarth's response [2] to the FCA's 2023 engagement papers, and make the additional comments set out below.

As the FCA recognises in CP24/12, "*disclosure of consistent, reliable, sustainability-related information in the prospectus is important to ensure that investors have a full understanding of the prospects of the companies in which they invest and can make decisions aligned with their risk appetite and capital allocation preferences. In turn, this can support market functioning by enabling more accurate pricing.*"[3] The rules for sustainability disclosures in the annual reporting of listed companies have advanced ahead of the prospectus disclosure regime. This is a missed opportunity for the regulator to ensure the provision of material, decision-useful sustainability information to the market at the point it has most leverage over regulated companies – i.e. when they apply to list. The FCA's proposals to improve the provision of sustainability information at the point of listing are a welcome first step to fill that gap.

The reforms will also help provide clarity on the information that investors are expected to disclose, and therefore increase the usefulness of the disclosures to stakeholders. As the FCA originally acknowledged in Engagement Paper 1 (paras. 74 and 75), this clarity is currently lacking, leading to inadequate sustainability disclosures in the prospectus.[4]

However, we make the following comments regarding the design of the new requirements:

- We agree that the identification of climate-related risk factors is a convenient trigger for the additional climate-related disclosures envisaged in CP24/12. However, in our view the identification of climate-related risks and opportunities and the consequential provision of additional climate-related disclosure should be on a 'comply or explain' basis in line with TCFD reporting requirements for listed companies. This would provide investors and other stakeholders with useful information in the event that a company does not consider climate change to pose material risks. For some highly climate-exposed sectors (such as oil and gas), for example, this would be a startling conclusion that would require careful explanation.
- In our view the framework for additional climate disclosures in the prospectus should be set up to align more fully with the TCFD recommendations and the disclosures provided for in ISSB S2 (which are currently referred to in para. 6.12 of CP24/12 and PRM 4.6.3 on a "may be of assistance" basis). This would minimise any gap between the information provided in the prospectus and that which companies are required to provide in their periodic disclosures, once listed. It would also

[2] ClientEarth's response to the FCA's 2023 engagement papers is available here: FCA Engagement Papers 1-4: New regime for public offers and admissions to trading (clientearth.org).
[3] Para. 6.3 of CP24/12.
[4] See also pp.4-5 of ClientEarth's response to the FCA's 2023 engagement papers.

better leverage the huge international multi-stakeholder effort to devise appropriate sustainability disclosure standards represented in the work of the TCFD and the ISSB.[5] We suggest that the required disclosures in the PRM are built directly by reference to these standards, and applied on a 'comply or explain' or mandatory basis.

Question 32: How do you consider our proposed requirements on sustainability-related disclosures could affect the cost of producing a prospectus?

We strongly endorse the FCA's assessment that these proposals are proportionate and appropriate given the materiality of climate-related risks for issuers and investors, in light of the fact that "*under Listing Principle 1, listed companies are already expected to take reasonable steps to establish and maintain adequate procedures, systems and controls to enable them to comply with their obligations, including the requirement to include within their annual financial report a statement on whether they have made disclosures consistent with the TCFD Recommendations and Recommended Disclosures*" (para. 619 of CP24/12). We echo again the FCA's observation in Engagement Paper 1 (para. 78) that "*if these requirements are aligned with what issuers would later be required to produce in the annual report, the additional burden [on companies] could be minimised*". If the effect of the proposals is to accelerate by one reporting cycle the time at which issuers are required to provide adequate climate-related information to the market, that is a cost that is entirely justified.

In any event, given that the cost of listing, including all fees, can generally range from 5% to 15% of the gross proceeds raised[6], we would expect the marginal cost of providing the proposed climate disclosures to be manageable.

Paragraph 6.19 of CP24/12 also mentions the potential impact on issuers' choice of market. In this regard, we strongly recognise the FCA's statement of principle in para. 2.40 to the effect that "*international competitiveness can also be supported by maintaining our high standards. Well-regulated markets are necessary for investors to have confidence in the fairness and effectiveness of the market when choosing where to deploy their capital. We therefore have sought to maintain these key protections for investors through the high quality, comprehensive disclosure that is an integral feature of our current regime*."

The provision of adequate sustainability information at the point of listing is a key element of the competitiveness-through-standards acknowledged here by the FCA. We repeat the comments to this effect made in our response to the FCA's 2023 engagement papers.[7]

Question 33: Do you have any views on the importance that investors and other readers of prospectuses would place on the additional climate-related information disclosed under the proposed climate disclosure rule?

We repeat comments we have made to the FCA previously regarding the materiality of climate and sustainability information to investment decision-making.[8] We add that enhanced sustainability

[5] See further p.7 of ClientEarth's response to the FCA's 2023 engagement papers.
[6] As documented in this LSEG blog: The cost of listing in 1986 versus today, and the role of the Prospectus | Issuer Services | LSEG (lsegissuerservices.com).
[7] See p.3 of ClientEarth's response to the FCA's 2023 engagement papers.
[8] See pp. 6-7 of ClientEarth's response to the FCA's 2023 engagement papers: FCA Engagement Papers 1-4: New regime for public offers and admissions to trading (clientearth.org).

disclosures at the point of listing (on as rigorous a basis as possible) would help FCA-regulated asset owners comply with their own mandatory TCFD reporting requirements.

Question 34: Do you agree that our proposed climate disclosure rule should apply to issuers of equity securities and issuers of depositary receipts only, with other securities addressed through the Technical Note? Y/N. Please give your reasons.

No – in our view the provision of adequate decision-relevant climate-related information the point of issuance is equally relevant to the debt market.

This is particularly salient given the recent LSEG report highlighting that around $3.2 trillion of debt from high-carbon companies (commodities and utilities issuers) is due to be refinanced over the coming years[9]. In paragraph 6.23 of CP 24/12, the FCA states that, *"the wider variety of issuers and securities in [the debt] market means these issues may vary in importance and disclosure of this information may not be relevant in all cases."* However, the huge volume of impending refinancing by high-carbon companies brings the climate risk associated with investment in those companies sharply into focus for investors (including investors in relatively short-term debt instruments). To the extent distinctions must be made, in our view it is essential that high-carbon companies (including fossil fuel companies) are required to make adequate climate-related disclosures in relation to debt issuances and refinancing, so that the climate risk inherent in these high-carbon issuances can be priced effectively and investors can make fully informed allocation decisions.

For similar reasons, we consider it essential that the FCA considers how best to implement the 'mineral company' specific proposals set out below in response to Question 40 in a manner that carries through into debt markets and debt issuance documents. We would be pleased to arrange further opportunities to explore this aspect of the reforms.

Question 35: Do you agree with the proposed minimum climate-related disclosures in the Annexes to the PRM? Y/N. Please give your reasons. If not, what should be changed?

Not fully – please see our response to Question 31. In our view, aligning the required disclosures directly with TCFD and ISSB would be more effective to ensure the rigour and comparability of the information disclosed. This goes beyond the high level categories common to TCFD and ISSB.

Question 36: Do you agree with our proposed approach to transition plans? Y/N. Please give your reasons. If your reasons relate to cost or other concerns, please provide further detail.

Yes – we broadly support the FCA's approach to transition plan disclosure in CP24/12. It is, however, ClientEarth's view that the proposals as currently formulated fall short of the stated policy intent. We have the following comments on the proposals:

- Firstly, listing should be a *trigger* for transition planning. The current proposal is that *if* the issuer has published a transition plan *and* the contents are material, a summary of the transition plan

[9] LSEG report, Tracing carbon-intensive debt (lseg.com). Also, see Bloomberg's coverage of this report: A $3.2 Trillion Refinancing Wall Looms for High-Carbon Issuers | Financial Post.

should be included in the prospectus together with details of where it may be located and inspected. This aligns with the requirement in IFRS S2 (para. 14(a)(iv) for entities to disclose "*any climate-related transition plan the entity has*", but sits uncomfortably alongside the Labour Government's manifesto commitment to "[*mandate*] *UK-regulated financial institutions – including banks, asset managers, pension funds, and insurers – and FTSE 100 companies to develop and implement credible transition plans that align with the 1.5°C goal of the Paris Agreement*".

If the UK roll-out of mandatory transition planning mirrors the approach to TCFD-aligned disclosure, we would expect those companies that have 'already' published a transition plan to eventually include: companies that are already UK listed; large UK private companies and LLPs; and FCA-regulated financial institutions. However, in the meantime, there are likely to be companies applying to access regulated UK markets that do not already have a transition plan in place. The position of foreign companies applying to list in the UK (which are not subject to local mandatory transition planning requirements) must also be considered.

In our view, it would be a wasted opportunity to further the UK's green finance policy objectives if such companies were not required to develop a transition plan and disclose details in their prospectus. This approach also risks perverse incentives, because it would make listing more arduous for those companies that already have a transition plan in place (and therefore have to make additional disclosures) – when those are exactly the companies that should be facilitated to access UK regulated markets. Companies without a transition plan in place would (perversely) have an easier ride. It would be a far more effective use of the regulatory levers available to the FCA, aligned with the Government's stated policy intentions, for the publication of the prospectus to *trigger* a standalone requirement for companies to develop and disclose a (1.5°C-aligned) transition plan, even if they don't already have one.

- Additionally, at least in relation to companies that *already* have a transition plan, there is no need for the materiality qualifier suggested by the FCA. In our view, if a company has a robust transition plan, it is likely to be so enmeshed in the company's strategy and business planning as to always be material to investors.

The FCA states in para. 6.34 of CP24/12 its proposal that transition plans should be eligible to be considered as protected forward-looking statements (**PFLS**). This needs to be approached with caution.

- Firstly, it is out of step with the principle that disclosures which are mandatory and required by the Annexes to the PRM should generally not be considered eligible to be PFLS. This will be particularly relevant if the proposals are adjusted to make the prospectus a trigger for a freestanding obligation to disclose the transition plan (as recommended above). Any deviations from this principle (i.e. making certain aspects of the transition plan eligible as PFLS) should be targeted and specifically justified. The broad assertion that transition plans are primarily forward looking does not provide adequate justification.

- Secondly, experience has shown that current practice in relation to corporate net zero commitments and transition planning represents a market failure marred by low integrity, misalignment with international climate goals, unjustified emissions Scope exclusions, overreliance on offsetting, false solutions and speculative technologies, and in some cases greenwashing.[10] In that context, the risks associated with PFLS status are elevated in that "*less stringent liability would undermine existing protections on certain key information for investors*".[11] It is important that the liability standard is calibrated to allow for accountability where corporate transition plans exhibit flaws such as those listed above, and are misleading as a result. Many of the features most susceptible to 'gaming' or failure are not necessarily forward looking (in the sense that "*verification as to the truth, correctness, and completeness of the statement can only be carried out by reference to an event or set of circumstances that occurs [in the future]*"[12]). For instance, a claim to be net zero committed can be undermined *today* if Scope 3 emissions are omitted, the planned actions disclosed cannot reasonably be expected to deliver against stated climate targets or the plan relies overly on offsets which clearly displace emissions reductions. Deficiencies of this nature have nothing to do with future circumstances which cannot yet be assessed, they speak to a lack of integrity in the plan *today*. We urge the FCA to carefully apply PFLS criteria to each element of transition planning to ensure that its approach does not extinguish the possibility for effective accountability in situations of this nature (where we would argue the negligence standard of liability is wholly appropriate).

- In particular, the draft PRM currently provides at 8.1.4 that items 5.8.2 ("A description of the actual and potential impacts of climate-related risks and opportunities on the issuer's businesses, strategy, and financial planning"), 5.8.3 ("If the issuer has published a transition plan, where the contents are material, a summary of key information about the transition plan and where it may be located and inspected") and 5.8.5 ("If material, a description of the metrics and targets used to assess and manage") should be excluded from the general rule that disclosures which are mandatory and required by the Annexes to the PRM (as these disclosures are) should generally not be considered eligible to be PFLS.

  We return again to the FCA's point that where disclosure is mandatory, there is no benefit to investors by allowing such statements to be included within the scope of PFLS[13]. In our view, the same reasoning should apply in respect of these sustainability-related disclosures: given that these disclosures would be mandatory under current proposals, investors will receive no benefit from these statements being designated as PFLS. Conversely, such a designation would only serve to weaken the recourse that investors might have to an issuer in the event that they suffer loss and should be carefully and specifically justified by the FCA.[14]

[10] See, for example, the annual Corporate Climate Responsibility Monitor reports produced by New Climate Institute: Corporate Climate Responsibility Monitor - Carbon Market Watch. The 2024 report is available here: Corporate Climate Responsibility Monitor - 2024 - Carbon Market Watch. See also the latest annual findings of the CA100+ investor coalition assessments: Latest Climate Action 100+ Benchmark shows decarbonisation is underway for many of the world's largest corporate emitters, with a need for stronger climate transition action plans | Climate Action 100+.
[11] See para. 7.36 of CP24/12.
[12] See para. 7.19 of CP24/12.
[13] See para. 7.36 of CP24/12.
[14] Though we note that the additional PFLS criteria set out in Chapter 7 would need to apply and in some circumstances mitigate this effect.

Specialist issuers – mineral companies

Question 40: Should we provide additional guidance relating to climate disclosures for mineral companies (including mining and oil and gas)? Please give your reasoning, and if so, how should we do so?

We refer to:

- ClientEarth's response[15] to the FCA's 2023 engagement papers[16] on the new public offers and admissions to trading regime, in which we explained the need for additional prospectus disclosures for "mineral companies" and advocated for requirements for the resources and reserves assessments provided in the Competent Person's Report (**CPR**) to incorporate tests against climate constraints;
- The June 2024 joint submission by ClientEarth and Carbon Tracker to the Society of Petroleum Engineers regarding the proposed update to the Petroleum Resources Management System (**PRMS**)[17], advocating for climate constraints to be integrated into the PRMS methodology[18]; and
- The investor briefing published jointly by ClientEarth and Carbon Tracker in which these issues and the opportunity for reform are explained to the investor community[19].

The detailed proposals outlined in these documents remain relevant to the FCA's current consultation question and **we ask that you have reference to these documents and treat them as incorporated in full into our submissions in relation to CP24/12**.

It is essential that the FCA introduces additional climate disclosure requirements for mineral companies. In this regard we welcome the FCA's recognition of "*the importance of investors having sufficient information in prospectuses to assess the company's prospects and that this could include the impact of future climate scenarios and policy trajectories on the ability to extract resources in a financially sustainable manner*."[20]

The FCA's decision, in response to submissions on its 2023 engagement papers from ClientEarth and Carbon Tracker, to include this topic within the current consultation is an essential and welcome first step in ensuring that the prospectus content rules applicable in the UK are fit for purpose in a world transitioning away from fossil fuels. The UK's climate commitments and ambitions for a net zero financial centre make reform in this area all the more necessary and pressing.

The FCA must now develop effective and proportionate concrete proposals for reform of these requirements, which lead to adequate consideration of climate risk in reserves estimations and disclosures, providing investors with the information they need to make reliable, fully informed investment decisions.

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[15] ClientEarth's response to the engagement papers is available here: FCA Engagement Papers 1-4: New regime for public offers and admissions to trading (clientearth.org). See pp.10-16 for submissions in relation to "mineral company" disclosures and the Competent Person's Report.
[16] See Engagement feedback on the new public offers and admissions to trading regime | FCA.
[17] Petroleum Reserves and Resources Definitions (spe.org).
[18] The ClientEarth/Carbon Tracker submission to the Society of Petroleum Engineers is available here: Joint Submission to the Society of Petroleum Engineers regarding PRMS | ClientEarth. This was shared with the FCA over email on 9 July 2024.
[19] The ClientEarth/Carbon Tracker investor briefing is available here: FCA Consultation on Reforming Fossil Fuel Prospectus (carbontracker.org).
[20] CP24/12, para. 6.49.

Building on the proposals outlined in the documents listed above, in this response to Question 40 we address each of the bullets in paragraph 6.50 of CP24/12 in turn.

Additional climate-related disclosures for mining, oil and gas companies are needed

We have comprehensively explained the case for additional climate-related disclosures for mining, oil and gas companies in the documents listed above. Please see:

- Pages 10 to 16 of the engagement papers response;
- Pages 5 to 7 of the SPE submissions; and
- Pages 2 to 6 of the investor briefing.

In summary, reform in this area is necessary to provide investors with a transparent and externally verified picture of the viability of companies' fossil fuel reserves in a carbon-constrained world, so that they can make informed investment decisions, manage their risk exposure and discharge their fiduciary duties to their beneficiaries.[21]

Such reform would help steer the allocation of capital towards the activity in the fossil fuel sector that is most consistent with achievement of the Paris Agreement goals and the low carbon transition. Further, it will help the market identify and address the accumulation of 'unburnable carbon' and stranded assets on the London Stock Exchange (**LSE**) so that the associated financial and systemic risk can be priced and managed efficiently.

Without an independent stress test of which reserves are likely or unlikely to be consistent with the Paris Climate Agreement temperature goals (and the corresponding global policy response), companies and through them their shareholders, face the risk of stranded fossil fuel assets as climate policy action and the energy transition accelerates.[22] Carbon Tracker's '*Unburnable Carbon: Ten Years on*' report has shown that the fossil fuel reserves held by listed companies on the world's stock exchanges already greatly exceed those that can be burned even under the most pessimistic scenario, i.e. exceeding 3C[23]. In this context, risk accumulates in the handful of stock exchanges that play an outsized role in capital raising by fossil fuel companies and are transmitted to investors – including the LSE[24] – and for the investors exposed to those exchanges.[25]

Investors in the LSE face concentrated stranded asset risk as a result, while the exchange itself facilitates the transactions which support the continued expansion of the fossil fuel industry - transactions that are

[21] On the need for investment fiduciaries to take account of climate goals in their investment decisions, see: NZLA, '*Sustainable Fiduciary Duties*' (18 September 2024).
[22] The UN Intergovernmental Panel on Climate Change (**IPCC**) confirmed in 2022 that projected CO2 emissions from existing and planned fossil fuel infrastructure (without additional abatement) will exceed levels consistent with pathways that limit global warming to 1.5°C with no or limited overshoot (see IPCC AR6 WGIII SPM at B.7.). The implication is that many proven fossil fuel reserves must be left in the ground if the world is to stand any chance of meeting its climate goals. A recent study has suggested that in order to limit global warming to 1.5°C, up to 40% of fossil fuel reserves currently under development will need to be left in the ground. See '*Existing fossil fuel extraction would warm the world beyond 1.5 °C*' (Trout et al., 17 May 2022, Environ. Res. Lett. 17).
[23] See '*Unburnable Carbon: Ten Years On*' (2022).
[24] The emissions embedded on the LSE have been estimated to be 30 times greater than those of the UK's own fossil fuel reserves, and ten times the UK's carbon budget for 2023-2037. See p.12 of Carbon Tracker, '*Unburnable Carbon: Ten Years On*' (2022). The concept of embedded emissions in this context (meaning the carbon potential of known fossil fuel reserves held by companies listed on the LSE) is explained further on pages 10 – 14 of the report.
[25] Carbon Tracker's '*Loading the DICE Against Pensions*' (July 2023) is one of a number of recent studies and publications highlighting that financial institutions may be drastically underestimating the financial risk associated with given degrees of global warming, concluding that "*a wealth-damaging correction or "Minsky Moment" cannot be ruled out, and is virtually inevitable*".

not only bad for the planet, but generate risk for investors and the stability of markets. Nevertheless, these transactions continue – the largest IPO on the LSE in 2022 was that of Ithaca Energy plc, a pure-play North Sea oil and gas producer with interests in the most significant development projects in the region.[26]

The climate risk for investors exposed to the FTSE indices increases as a result of transactions like this - if a significant portion of the fossil fuel reserves represented on the LSE prove 'unburnable', the shock to investment value and financial integrity in the UK could be dramatic.

Requiring a climate test before reserves are considered 'viable' could help shed light on this issue and allow investors to react (including by deciding not to invest in new market entrants) before these risks crystallise. Reform that carries over (directly or indirectly) into debt markets would also be timely reform given the recent LSEG report highlighting that around $3.2 trillion of debt from high-carbon companies (commodities and utilities issuers) is due to be refinanced over the coming years[27]. Provided the new disclosures are implemented so that they follow through into annual reports and bond prospectuses, the market would be able to reprice risks in refinancing bonds with greater clarity.

Wider climate-related reporting requirements do not provide sufficient transparency

Wider climate-related reporting requirements are insufficient to provide the necessary transparency but more importantly, the suggested reforms would complement the wider requirements well.

Wider climate-related reporting requirements (including TCFD-aligned reporting for UK listed and large companies and regulated financial institutions; and developing transition planning requirements and standards) play a valuable role in establishing a baseline for the provision of corporate disclosures which help stakeholders understand the climate-related risks, impacts and strategies of businesses in any sector.

Clearly, however, they are tools of a very different nature to economic and technical fossil fuel reserves assessments, and designed to solve a very different problem. The existing frameworks provide for broad disclosures on risk and strategy that allow for a lot of discretion, contingency and dependency (so long as this is adequately explained in disclosures). They are designed to improve the rigour with which climate risk is considered in business planning, and the quality of disclosures provided to stakeholders on the same. But business planning is very different to the technical assessment of the viability of fossil reserves, which can be a valuable *input into* business planning.

The frameworks are limited insofar as they do not mandate corresponding rigour to be injected into the specific estimation, valuation and disclosure methodologies that are integral to certain sectors such as the disclosure guidance provided in TN619.1 and the rules surrounding the CPR.

As a result, broad based climate disclosures will not on their own ensure that independent testing of reserves is fit for purpose. A CPR process that remains blind to climate constraints would continue to undermine the value of TCFD scenario planning and transition plans in the coal, oil and gas sectors to the extent that it supports viability assessments and valuations that are inconsistent with: (a) the pace of transition, the policy response to the Paris Agreement and physical climate risk; and / or (b) the company's overall approach to transition as stated / claimed in TCFD and transition plan disclosures.

Similar considerations apply to the proposals set out in CP24/12 for: (a) enhanced climate disclosures for issuers identifying climate as a material risk; and (b) transition plan summary disclosures in the prospectus,

[26] It is worth noting details of Ithaca's post-listing performance: Ithaca Energy sees earnings slide amid dwindling production | This is Money; Boss of North Sea oil and gas producer Ithaca quits (ft.com).
[27] LSEG report, Tracing carbon-intensive debt (lseg.com). Also, see Bloomberg's coverage of this report: A $3.2 Trillion Refinancing Wall Looms for High-Carbon Issuers | Financial Post.

which are very positive but will not ensure the rigour of reserves estimations without the development of more direct requirements.

Climate-sensitive reserves estimation would align with and support broader climate disclosure requirements

Conversely, developing requirements for high integrity testing of the viability of fossil reserves would be an effective complement to the broader disclosures required under TCFD and transition planning requirements. For example, the Transition Plan Taskforce's disclosure guidance for the oil and gas sector[28] requires a company to disclose:

- *any objectives and priorities, including timeframes, to phase-down and phase-out any unabated fossil fuel-related business and diversify towards products and services which support a transition to a low-carbon, climate-resilient economy* (p.20);
- *how it plans to mitigate potential climate-related risks, originating from its business model, such as stranded asset risks, litigation risks, transferred emissions and other risks from former or sold assets and access to financial and capital markets* (p.22);
- *the role of new oil and gas exploration and production assets in its business model, stating any impact these have on its Strategic Ambition. This should consider disclosure of their location, and projected absolute emissions and intensity calculated over their operating life* (p.22);
- *assumptions which inform or affect its transition plan, including those relating to…oil and gas demand and pricing; GHG emissions prices (including methane pricing);… expected role of GHG neutralising measures, including assumptions relating to permanence/ leakage;… physical risks and impacts of climate change* (p.23);
- *for entities with major projects in development, how risks (transition and physical), impacts, and mitigations, have been considered in financial planning for those projects* (p.27);
- *the target internal rate of return (IRR) for business segments as outlined above, including the 'breakeven' price, methodology, and any underlying assumptions for the relevant commodity (oil, gas, other) to achieve the stated target internal rate of return ('IRR')* (p.27);
- *financial implications of assumptions and external factors (section 1.3 Key assumptions and external factors) relating to transition. For example, an entity may disclose sensitivity of hydrocarbon reserve levels and/or refining capacity to future price projection scenarios that account for increasing economic costs of GHG emissions and other drivers of demand shift (such as electric vehicles or heat pumps)* (p.32);
- *The emissions potential of proven and probable reserves* (p.35).

A reserves estimation and CPR reporting framework which incorporates a test of the compatibility of the extraction of reserves with science-based climate mitigation pathways (i.e. **an atmospheric viability test** – see below) would be a critical input into each of these reporting lines and many others.

As such, climate-aware reserves reporting would support companies and directors in preparing their transition plan disclosures and assessing the resilience of their reserves to the low carbon transition and physical climate risk. The expert input provided in the CPR, in particular, would help support the rigour and

[28] TPT-Oil-and-Gas-Sector-Guidance.pdf (transitiontaskforce.net).

reliability of the corresponding transition plan disclosures listed above. On the other hand, allowing reserves estimation to proceed without consideration of climate constraints would potentially leave reserves disclosures isolated from, and inconsistent with, the sophisticated climate disclosures provided by the company in its climate and transition planning disclosures.

We make further comments in relation to the **consistency** between reserves reporting and other disclosures below.

Climate-related factors must be integrated into the Competent Person's Report

In light of the above, the FCA must introduce climate-related factors as recommended content to be considered as part of the CPR in TN619.1 Appendices II and III. As explained below, climate-related factors should, **in addition**, be introduced within the FCA's own requirements in TN619.1 which overlay the CPR itself. This is to ensure that the disclosure framework is robust should a particular regional CPR methodology prove to be inadequate in practice.

We have explained the need for this in the documents listed above. Please see specifically:

- Pages 10 to 16 of the engagement papers response;
- Pages 3 to 7 of the SPE submissions; and
- Pages 3 to 6 of the investor briefing.

As explained in those documents, the FCA's guidance currently requires the production (and inclusion in the prospectus) of a CPR prepared in line with one of a number of 'acceptable' third party methodologies listed in Appendix I of TN619.1.[29] For oil and gas companies[30], this includes the Petroleum Resources Management System (**PRMS**) published jointly by the Society of Petroleum Engineers (**SPE**), the World Petroleum Council, the American Association of Petroleum Geologists and the Society of Petroleum Evaluation Engineers, as amended, and equivalent standards established in Canada and Norway.

The FCA's rules then go on to stipulate that the CPR must contain information on the company's "mineral projects" having regard to the information set out in Appendix II (for mining projects) and Appendix III (for oil and gas projects).[31]

The PRMS methodology is used to test and classify fossil resources and reserves according to their ability to be extracted technically and sold commercially. This is an economic, geological and technical assessment which is then reported in the CPR. Although there are a number of required disclosures (both within PRMS and the FCA's own requirements) that could in theory be interpreted as requiring an explanation of how climate-related matters affect this assessment[32], they are not applied this way in

[29] See para. 133(i)(c) of TN619.1.
[30] Appendix I also lists applicable codes of practice for reporting by mining companies, including the Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves (the **JORC Code**), and three valuation standards. We do not analyse the JORC code, or other mining or valuation codes, for the purposes of this response, but similar considerations apply as we have identified in relation to PRMS.
[31] See para. para. 133(i)(d) of TN619.1.
[32] For example:

- PRMS requires reserves and resources to be evaluated based on a number of 'defined conditions'. These include factors that affect commerciality such as "*decision hurdle rates; commodity prices; operating and capital costs; technical subsurface parameters; marketing, sales route(s); environmental, governmental, legal, and social factors; and timing issues*" (See paras. 1.2.0.10 and 3.0.0.2 and p.40 of PRMS 2018). PRMS also lists in various places "environmental factors" among the factors which may influence the assessment of commerciality (See paras. 1.2.0.10, 3.0.0.2, 3.1.0.1 and p.40 of PRMS 2018).

practice. Moreover, neither the customary CPR reporting standards nor the FCA's own rules include a free-standing climate test against the remaining carbon budget for fossil fuels to be counted as viable reserves. Nor is there any specific requirement to explain how climate-related matters (including carbon budgets and economic transition) have been taken into account in the financial assessment of whether reserves are commercially viable.

As a result, the CPR and mineral company disclosures are presently drawn up with little to no apparent regard for the impact of the transition to renewable sources of energy, global decarbonisation efforts or remaining carbon budgets on the viability of the commercial extraction of fossil fuel companies' reserves.

This deprives investors of vital transparency, necessary to enable investors to make reasoned judgements about the valuation of resource-dependent fossil fuel businesses and to make informed investments decisions. Allowing the impact of climate-related matters on reserves viability to remain obscure also permits underappreciated climate risk – and potentially stranded assets – to accumulate in investment portfolios in the UK and capital markets more broadly.

The FCA effectively delegates the standards which govern the preparation of the CPR to industry bodies (including the SPE and the PRMS methodology). In order to discharge its own duties, the FCA must have confidence that these standards are fit for purpose as the world transitions and financial markets and investors adapt. This is not possible if the applicable standards are blind to climate constraints – making them clearly inadequate.

The SPE's own Climate Change Task Force recognises the current limitations of the SPE's ability to ensure that climate constraints are adequately taken into account through PRMS evaluations, stating:

> "*Given that SPE does not have technical expertise or mandate for assessing climate science or guiding policy, the Task Force does not recommend that SPE develop a public position statement on climate science and climate change*."[33]

This is an existential problem for the credibility of the current PRMS framework, and others like it. Relying on standards which are climate-blind makes it impossible for the FCA to discharge its own duties, and so the FCA must adapt its expectations for the standard setters and their methodologies. Reform to the TN619.1 rules should therefore be conducted in a way that requires the PRMS and other methodologies to be updated to take climate constraints into account (through an atmospheric viability test – see below), through the rules which apply to the preparation of the CPR.

In order to safeguard the rigour of the new reserves reporting regime in the event that one of the third party standards proves deficient in practice, we suggest that the FCA also establish an explicit requirement for climate constraints to be taken into account which *overlays* the rules governing the preparation of the CPR. In the language of TN619.1, acknowledging that this may be replaced rather than updated, this could be through specific lines added to paragraph 132 (in addition to more granular requirements for the CPR process imposed via paragraph 133 and Appendices I to III).

- The FCA's current rules suggest that resources and reserves disclosures in the Competent Person's Report should include "*supporting assumptions including commodity prices, operating cost assumptions and other modifying factors used to derive reserve statements"* and "*a statement setting out any additional information required for a proper appraisal of any special factors affecting the exploration or extraction businesses of the company (for example in the polar regions where seasonality is a special factor)*" (Appendix II, paras. (iii)(5) and (ix) of TN619.1).

[33] Climate Change Task Force Recommendation (spe.org).

Designing the atmospheric viability test

In the consultation, the FCA has identified a clear pathway to enhance fossil fuel prospectus disclosures to better account for the impact of the energy transition on the viability of fossil fuel resources and reserves, which could be achieved through proportionate adjustments to the current rules. We support the development of requirements for 'mineral company' disclosures and or the CPR to incorporate:

a. **a dedicated test of the 'atmospheric viability' of fossil fuel resources reserves**, based on remaining carbon budgets (alongside existing tests of their economic and technical recoverability);

b. **broader disclosure of the impact of the energy transition on the financial viability of company resources and reserves**, and on the assumptions and projections that underpin the assessment (such as oil and gas price and demand assumptions).

A dedicated test of the **atmospheric viability** of fossil fuel resources and reserves would assess whether:

a. there is space in the atmosphere for the reserves in question, once combusted, taking into account the best and most credible scientific estimates of the remaining carbon budget that are available (and projected global demands on it) in reference scenarios, and a scientific assessment of the likely emissions released once the reserves are combusted; and

b. the extraction of its reserves is otherwise consistent with credible science-based pathways to limiting global temperature rise consistent with the Paris Agreement[34].

The design and implementation of this test requires a number of design choices to be made by the FCA. The options for designing an effective atmospheric viability test should be fully worked through. However, one option which could form the basis for further discussions would be for the reference scenarios considered in the assessment to be used to identify a per barrel break-even price (or equivalent measure) compatible with the carbon budget associated with the relevant scenario. If petroleum resources under assessment require a break-even price which exceeds the limit imposed by the relevant reference scenario, they would not be considered compatible with the scenario or the carbon budget implied by the scenario.[35][36] In any event, for new projects, the test should also adhere to the principle that new oil and gas projects are incompatible with, or at least not required in, scenarios compatible with holding warming to 1.5°C.[37]

There are similarly a range of possible approaches to the consequences of viability / non-viability. At one end of the spectrum is an outright assessment of viability against specified temperature pathways.

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[34] Or any successor to the Paris Agreement goal that is subsequently agreed.
[35] By way of illustration only, the IEA's 'World Energy Outlook 2023' (October 2023) projected that "*In the NZE Scenario, oil and gas prices quickly fall to the costs of the marginal project required to meet falling demand, which is around USD 40/barrel for oil in 2030, before declining further to USD 25/barrel in 2050. These prices cover the operating expenses to lift oil and gas out of the field of the marginal producer, the capital expenditure and operating cost required in emissions reduction technologies, as well as upstream taxes*." (p.96). Carbon Tracker Initiative's least-cost analysis provides one example of a framework for assessing marginal breakeven prices of potential projects relevant to the classification of reserves. See: Paris Maligned II - Carbon Tracker Initiative for details. Under this methodology, the marginal breakeven prices for potential oil and gas projects calculated for global oil and gas supply and the IEA's World Energy Outlook 2023 are ~$40/bbl for the APS demand and ~$65 for the STEPS demand. There is no space for new projects in the modelled NZE scenario.
[36] We would expect this assessment and reporting to be achievable without raising significant confidentiality concerns. If they do arise, however, projects could be stress tested for viability through disclosure of project capex and costs falling within different break-even price bandings. It would follow that projects and associated capex and costs that are at within the lowest break-even price bandings are more likely to fall within the remaining carbon budget for a given climate scenario.
[37] 4 See the IEA's projection that in the net zero scenario, "*investment in existing fields is needed to ensure that supply does not decline faster than demand, but no new conventional long lead time oil and gas projects are developed after 2023*". See p.135 of IEA, 'World Energy Outlook 2023' (October 2023), available here.

Another option would be a requirement for the 'atmospheric viability' of reserves (including assessment of a viable break-even price) to be assessed against a range of authoritative science-based climate and energy sector scenarios[38]. Assessors would be required to justify their choice of scenarios and in all circumstances would be required include at least one scenario compatible with 1.5°C / NZ 2050.[39] There may be advantages to the FCA specifying one authoritative 1.5°C / NZ 2050 scenario to be used, in terms of the consistency and comparability of assessments – that is another design choice that will need to be resolved. Resources and reserves would then be classified against the temperature scenario in which they become viable. For anything other than a 1.5°C scenario, this would amount to a warning label stating clearly that the reserves are only viable at levels of global warming that are dangerous to human health, the environment and financial stability. We consider this a minimum viable approach to the reforms.

Current CPR requirements do not lead to sufficient transparency and consistency

The current disclosure requirements for 'mineral company' prospectus disclosures do not lead to sufficient transparency about the assumptions underlying specialist issuers' and competent persons' assessments of the viability of reserves, including the impact of future climate scenarios. Nor are they adequate to ensure that the assumptions and analysis presented in the CPR are consistent with information provided in wider prospectus disclosures, as required by TN619.1 III.2 paragraph 133(iii), and with wider climate reporting such as TCFD disclosures or climate scenario analysis presented by the company.

On **transparency**, we note simply that the CPRs we have been able to review make no mention of climate-related considerations. This reflects the situation described above – neither the reserves estimation methodologies or the FCA's own rules currently require this explicitly. See, for example, the CPR included in Ithaca Energy plc's 2022 IPO prospectus (at p.472).[40] The CPR, prepared by Netherland, Sewell & Associates Inc.[41] makes no reference to climate change or transition. Illustrating the issues with the current regime described in these submissions, it does note that:

> "*The estimates in this report have been prepared in accordance with the definitions and guidelines set forth in the 2018 Petroleum Resources Management System (PRMS) approved by the Society of Petroleum Engineers (SPE) and in accordance with the recommendations of the Financial Conduct Authority (FCA), as set out in Primary Market Technical Note 619.1 – the Guidelines on disclosure requirements under the Prospectus Regulation and Guidance on specialist issuers published by the FCA*." (p.472).

The CPR also notes explicitly that "*As requested, this report has been prepared using oil, NGL, and gas price parameters specified by Ithaca*" (p.475 and p.730). Comparing these price parameters against those implied by the NZE and STEPS scenarios provided by the IEA shows that these prices are not compatible with IEA projections for Paris-aligned transition scenarios, or even those based on current government policies. For example, the Ithaca CPR is based on an oil price of $112 per barrel in 2040, rising 2% per year thereafter. In its World Energy Outlook 2024[42], the IEA's NZE scenario implies an oil price of $30 per barrel in 2040, falling to $25 per barrel in 2050. Even in the STEPS scenario, oil prices remain below 2023

[38] Reference scenarios would include the International Energy Agency's (IEA) Net Zero emissions by 2050 (NZE), Announced Pledges (APS) and Stated Policies (STEPS) scenarios.
[39] See No new fossil fuel projects: The norm we need | Science for further exploration of why this is required.
[40] Ithaca's 2022 IPO prospectus is available here: Ithaca Energy plc - Final Prospectus.pdf (fra1.cdn.digitaloceanspaces.com).
[41] Home - Netherland, Sewell & Associates (netherlandsewell.com). Please note that we provide this analysis of Ithaca's CPR by way of illustrative example only, not to imply that it is an outlier in terms of current practice or any specific breach of the currently applicable requirements.
[42] See World Energy Outlook 2024.

levels ($82 per barrel) through to 2050 (falling to $77 per barrel in 2040 and $75 per barrel in 2050).There is no suggestion in the CPR that a sensitivity analysis has been conducted against the prices implied by the IEA (or other) climate scenarios.

The closest the report comes to acknowledging the potential impact of transition is the generic disclaimer that "*Because of governmental policies and uncertainties of supply and demand, the sales rates, prices received, and costs incurred may vary from assumptions made while preparing this report*" (p. 476). This is plainly insufficient to give investors any meaningful information regarding the impact of climate constraints on the viability of the reserves covered in the report.

Likewise, there current rules do not ensure that the assumptions and analysis presented in the CPR are **consistent** with information provided in wider prospectus disclosures. The relevant requirement from TN619.1 provides that:

> *"Information on mineral resources and where applicable reserves and exploration results/prospects as well as other information of a scientific or technical nature included in prospectuses outside of the competent person's report (if one is included) must not be inconsistent with the information contained in the competent person's report."*

It is important to note that it is the information in the wider prospectus disclosures that must be consistent with the reserves estimation provided in the CPR (not the other way round). This makes sense because the CPR is designed to provide an independent expert *input* into how the company classifies, values and reports its reserves, and in so doing provide investors with comfort that a rigorous and supportable approach has been taken in light of relevant risks and uncertainties. This objective is not achieved if the report simply reflects assumptions and projections the company itself has already made.

The reforms we recommend are needed precisely because they would improve the quality and reliability of the CPR, and this would then feed through to underpin the rigour of the wider reserves reporting and climate disclosure framework (via accounting assumptions and estimates, reserves commentary elsewhere in the prospectus and climate and transition plan disclosures in relation to reserves and business strategy).

As things stand, the CPR process is not fit for purpose insofar as it fails to take into account climate constraints. This means that (theoretically) other prospectus disclosures *can* be consistent with the CPR without taking climate constraints, risks or projections into account – a bad outcome.

Nevertheless, we observe in practice considerable **inconsistency** between wider prospectus disclosures and the approach taken in the CPR. This arises as follows[43]:

i. The company identifies climate change as a category of material risk in its prospectus, but in very vague and general terms that give little insight into how specifically the company will be affected (something the FCA's proposals to require minimum climate disclosures in this situation would help remedy).

ii. The company may refer to various IEA scenarios (including STEPS and, hopefully, the NZE) in the section of its prospectus that discusses the prospects of its business. The best current reporting may provide some indication of how the company's business would be affected in these scenarios through sensitivity analysis.

[43] Please note that we have presented this pattern in abstract. If it would be helpful to the FCA, we could provide further commentary on specific examples privately.

iii. The company may also state in its financial reporting that climate-related matters have been taken into account.[44]

iv. However, neither climate risk considerations nor analysis against IEA (or other) scenarios feature in the CPR at all.

As a result, the prospectus (A) highlights climate risk to investors in vague terms that are not decision useful; and (B) fails to substantively integrate climate-factors into the CPR as a critical input into how reserves are assessed, valued and reported. This is plainly inconsistent. Added to this, the CPR is compromised insofar as it is based on favourable price assumptions selected by management rather than identified and tested independently by the Competent Person.

Finally, we note that, while enhanced climate and transition plan disclosures in the 'front end' of the prospectus are very welcome overall, they may compound the inconsistencies described above. This is because quality and granularity of the company's identification of climate matters should improve according to regulation and best practice guidance. Without commensurate improvements to the CPR process, the gulf between this reporting and the treatment of climate factors in reserves classification will grow.

Consistency benefits of reform to the CPR

Interpreting "consistency" in a different way, we make the additional comments below regarding the consistency of reform to the CPR process (to take climate constraints and atmospheric viability into account) with other climate disclosures, developing EU and ISSB disclosure requirements, and the UKs green and transition finance objectives:

- As explained above by reference to the TPT's guidance for oil and gas companies, developing requirements for high integrity testing of the viability of fossil reserves would be an effective complement to the broader disclosures required under TCFD and transition planning requirements.
- The suggested reforms would also align well with the development of global sustainability reporting standards (notably the EU and ISSB climate reporting frameworks) which require disclosure of locked-in or embedded greenhouse gas emissions, and sensitivity analysis of fossil fuel reserves against authoritative climate scenarios.[45]
- Enhanced reserves reporting would also serve the UK's objectives for the Net Zero Financial Centre and its ambitions for becoming a leading market for transition finance[46], including by supporting companies and financial institution investors to meet their climate reporting and transition plan

[44] Though we note the evidence of persistent, systemic failure to provide sufficient transparency on this, despite clear guidance from the IASB explaining how this should be done. See Carbon Tracker's latest '*Flying Blind*' (2024) report, available here: Flying Blind: In a Holding Pattern - Carbon Tracker Initiative.
[45] The climate disclosure standard (ESRS E1 *Climate Change*) under the EU's Corporate Sustainability Reporting Directive requires disclosure of "*a qualitative assessment of the potential locked-in GHG emissions from the undertaking's key assets and products. This shall include an explanation of if and how these emissions may jeopardise the achievement of the undertaking's GHG emission reduction targets and drive transition risk, and if applicable, an explanation of the undertaking's plans to manage its GHG-intensive and energy-intensive assets and products*" (see ESRS E1-1 para. 16(d)). The International Sustainability Standards Board's industry-specific guidance for oil and gas sector climate reporting under IFRS S2 asks companies to "*perform a sensitivity analysis of its reserves to determine how several future scenarios may affect the determination of whether the reserves are proved or probable*" and "*analyse the sensitivity of its current proven and probable reserves using the price trajectories published by the International Energy Agency (IEA) in its World Energy Outlook (WEO) publication*". It also requires Companies to consider disclosure of an estimate of the carbon dioxide emissions embedded in its proved hydrocarbon reserves (see pp.90-92 of IFRS-S2 *Industry-based Guidance on implementing Climate-related Disclosures*).
[46] See Scaling Transition Finance Report (theglobalcity.uk).

requirements in a manner which credibly explains their approach to transition insofar as it affects their reserves and resources.[47]

Potential costs are proportionate and manageable

In our view, the potential costs of introducing the new requirements in this are proportionate and manageable, whether or not the input of a qualified climate expert is required.

The economic aspects of the climate testing could be provided through a modest extension of the competent person's role, which builds on their existing expertise and experience. Qualified geologists and economists, and the well-established firms at which they work, should be more than capable of testing price and demand assumptions against authoritative climate scenarios, and there is an abundance of independent resources to help them do so.

As explained above, grappling with the impact of climate constraints on reserves estimations will create benefits in the rigour and reliability of other climate reporting. The costs involved must also be considered in that light. In any event, the benefit of providing investors with a more accurate assessment of risks far outweighs the modest increase in reporting costs.

[47] Noting the Labour Government's manifesto commitment to "*make the UK the green finance capital of the world, mandating UK-regulated financial institutions – including banks, asset managers, pension funds, and insurers – and FTSE 100 companies to develop and implement credible transition plans that align with the 1.5°C goal of the Paris Agreement.*"

Sustainability-labelled debt instruments

Question 41: Do you agree with the proposed new disclosure requirement and set of voluntary additional disclosures we are proposing to mitigate information gaps between bond frameworks (or similar documents) and prospectuses? Are there other disclosures that you think we should consider?

Question 42: Do you agree with the additional voluntary disclosures we are proposing to introduce in prospectuses for UoP bonds? Are there other disclosures that you think we should consider?

Question 43: Do you agree with the additional voluntary disclosures we are proposing to introduce in prospectuses for SLBs? Are there other disclosures that you think we should consider?

Please consider this a response to Questions 41, 42 and 43

We welcome the FCA's proposals to address the information gaps between bond frameworks and prospectuses to tackle the ongoing risks of misalignment between prospectus commitments and sustainability framework content that the FCA identified (EP4; para.57 and CP24/12 6.51). However, in our view the measures outlined in CP24/12 will be insufficient for the reasons we set out below.

Addressing the divergence between the bond framework and prospectus commitments

We refer to the proposed new disclosure requirement as described at CP24/12; paras.6.58-6.63. As the requirement is framed in those paragraphs, an issuer can meet the necessary information test (and thereby the disclosure requirement) with a mere statement as to whether the debt instrument has been marketed as 'green', 'social', 'sustainable' or 'sustainability-linked' and/or issued under a bond framework. This information is the minimum an investor or any other market participant could expect to know about a sustainability-labelled bond. While an explicit requirement for this information is not unwelcome, it would seem to add little (if anything) to the relevant existing Prospectus Regulation Rules requirements[48] and falls below the disclosure common in current market practice. The limited effect of this requirement risks undermining the use of such sustainability labelling without addressing the risk that the bond framework will contain different information from the prospectus and that an investor purchasing the bond will misunderstand the nature of the investment.

The need for regulatory requirements

The consultation's proposed disclosure *requirement* ends there, although there is a proposal for an additional voluntary element for all sustainability-labelled bonds: that the issuer would be "prompted (but not mandated)" (CP24/12; para.6.61) to include further disclosures, including the location of the bond framework and any second party opinion as to the alignment of the framework with industry principles.

Such disclosure – if the issuer chose to provide it – would not address the risk of the issuer's bond framework containing representations as to the issuer's green/social/sustainable approach which go

[48] Including, for example, PRR 2.1.1 UK

beyond the commitments in the prospectus. The disclosure would point the investor to the framework, and in doing so may make it *more* likely that the investor will misunderstand the nature of the investment by associating the non-contractual representations in the framework with the legally-binding prospectus document. Nor is this risk for the investor mitigated by issuers' deployment of second party opinions, which relate to the framework rather than the prospectus, and whose varied methodologies and utility have faced market scepticism.[49]

While we agree with the need for further additional, more specific, disclosures for UoP bonds and SLBs, we do not consider that the regulator's suggestion of additional disclosures on a voluntary basis will be effective in ensuring that investors have the information they need to take sustainability factors into account in their investment decisions.

As we set out in our response to EP4, disclosure of framework alignment to voluntary principles is widely used in labelled bonds already[50] and has failed to prevent the ongoing risks of misalignment between prospectus commitments and framework information that the FCA has identified (EP4; para.57 and CP24/12 6.51). As we stated in our response to EP4, the voluntary industry principles and guidance set out by ICMA and others provided a useful basis for a nascent market where products were being tried and proven, but as the FCA points out in CP24/12, the labelled bond market is now maturing[51] and the risks of weak, disparate and unenforceable commitments are becoming widespread.[52]

Investor demand for better disclosure and clearer commitments from issuers is not being met, and this failure is contributing to a year-on-year decline in investor demand in the SLB market since 2021, due to what ratings agency Moody's has called a 'quality gap'.[53] The social and sustainability bond markets have also declined, by 7% and 30% respectively between 2022 and 2023, we infer as a result of the same issues.[54] Regulatory requirements are therefore needed now to give the sustainability-labelled debt market the credibility that is essential for it to contribute the significant financial flows required to support the transition at the speed and scale required.

The market-wide risk outlined above cannot be addressed by the layering-on of an additional voluntary framework for disclosure. Nor can prospectus alignment with voluntary guidance, and/or verification by unregulated verifiers – even if an issuer chooses to provide this additional disclosure – add legal certainty or recourse for the investor in relation to the representations in the framework. As noted in our response to EP4, disclosure of net zero targets, strategies and transition plans under voluntary frameworks currently represents a market failure, which is seriously detrimental to investors' interests.

The disclosure requirement in CP 24/12 falls short of requiring the information that would support investor decision-making, and its adoption with mere voluntary additions would therefore constitute a missed opportunity for the FCA provide the certainty the market seeks. This is disappointing when, as the FCA points out in CP24/12, the regulator has a duty under s.1B(5) and 3B(c) of FSMA 2000 to have regard to contributing towards the Secretary of State achieving compliance with the net-zero emissions target under section 1 of the Climate Change Act 2008 and environmental targets under s.5 of the Environment Act 2021.

[49] As reported in *'Second-party opinions': a greenwash or just for show*, Eco-Business, 28 August 2024
[50] According to ICMA, its principles were referenced in an estimated 97% of sustainable bonds issued internationally in 2023. See *The Principles announce updated guidance* (icmagroup.org), accessed 19 September 2023
[51] FCA CP24/12 at para. 6.54
[52] Curtis et al., 2023, *Green Bonds, Empty Promises*, including at p.56
[53] As reported by Ahren Lester, '*SLBs: 2024 issuance slumps as issuer wariness grows*', Environmental Finance, 21 June 2024
[54] Climate Bonds Initiative, Sustainable Debt: Global State of the Market 2023, p. 3

Recommendations

To comply with the FCA's anti-greenwashing rule, firms should already be ensuring that their sustainability-related claims are fair, clear and not misleading (ESG 4.3.1R). In the context of a sustainability-labelled debt instrument, this should at a minimum include the following disclosures in the bond prospectus:

- the relevant sustainability terms of the bond framework;
- a statement as to where the full framework is published with a clear statement of the (lack of) legal status of that framework;
- confirmation that the bond framework has been independently and expertly verified, and by whom; and
- confirmation that ongoing verification will take place of the fulfilment of credible, science-based transition targets (or use of proceeds in line with such targets) by an independent expert at agreed points during the life of the bond. We recommend a rule to implement the FCA's own suggestion (EP4; para. 62) that issuers draw links to transition plans created in line with the Transition Plan Taskforce disclosure framework, which are likely to be material to investor decision-making.

The FCA should also require that sustainability-related claims and disclosures are not undermined by disclaimers, limiting language or structural loopholes like late-dated KPIs or call options[55] which detract from the value of the disclosures. A requirement for contractually binding commitments with clear accountability mechanisms would help to underpin the credibility and value of the sustainability-related claims and provide the certainty the market needs, as described below.

The need for contractually binding representations

Legal experts have noted the risk to investors arising from a lack of enforceability of climate-related promises in 'green' bonds (including green, sustainable, social and sustainability-linked bonds).[56] This lack of recourse creates potential risk for market participants, including asset owners, who must consider their legal duties in respect of their investment decision-making, and asset managers, who must consider their investment mandates. Mandatory disclosures should therefore specify whether, and how, sustainability terms are contractually reinforced. The IIGCC has recommended covenants and KPI linked bonds as methods to provide an accountability mechanism for investors during the lifetime of the bond.[57] Covenants can be included in the bond prospectus to attach clear, legal consequences to the UoP and/or the meeting of transition targets.[58] Such terms can aid the accurate pricing of labelled bonds and mitigate the systemic risk of ongoing mispricing in the market.

In practice, such terms lend themselves well to the structure of bond documentation: where an issuer has a base prospectus with an additional final terms document for each bond issuance, issuer-level covenants with transition plan targets should be suitable for the base prospectus, while specific use of proceeds restrictions or payment consequences like step-up coupons would be suited to the final terms of a particular issuance.

[55] The World Bank IFC, *Structural Loopholes in Sustainability-Linked Bonds*, 19 May 2022
[56] Corke et al., *Green Bonds Series: Part 4 - When 'Green' Bonds go Brown*, Lexology October 17, 2019
[57] IIGCC Net Zero Bondholder Stewardship Guidance p. 17; and Net Zero Investment Framework p. 18
[58] Corke et al., *Green Bonds Series: Part 4 - When 'Green' Bonds go Brown*, Lexology October 17, 2019; and Curtis et al., 2023, *Green Bonds, Empty Promises*

Requirements for admission to trading of non-equity securities on regulated markets

Question 27: Do you agree with our proposed approach to permit issuers to use future incorporation by reference of financial information, including the option for issuers to use supplementary prospectuses for this purpose? Y/N. Please give your reasons.

We do not agree with this proposed approach, which effectively removes the mandatory withdrawal rights investors currently have when a supplementary prospectus is issued that contains a significant new factor or material mistake/inaccuracy.[59] This is a clear erosion of investors' rights and a lessening of investor engagement power which is strongest at the point of issuance/reissuance.[60] Taking away these rights and influence would remove investors' ability to hold an issuer to account in relation to information that affects the issuer's sustainability profile, and it thereby increases greenwashing risk. The effect of this on investors' ability to mitigate climate risk and greenwashing risk, and the wider market's systemic risk, outweigh the benefit of flexibility for issuers that would be provided by removing this right.

In addition, we note that the FCA proposes to remove barriers for issuers of low denomination bonds, in order to reduce costs for issuing to retail investors, and that consultation on this is due later in the year. It is important to highlight that if the FCA adopts the proposals set out in this CP for dilution/erosion of wholesale investors' rights, this must not pave the way for corresponding dilution/erosion of retail investors' rights.

Question 28: Do you agree with our proposed approach to give issuers of non-equity securities more flexibility in relation to supplementary prospectuses? Y/N. Please give your reasons.

While we acknowledge the desire for increased flexibility and lower costs for issuers, we raise a note of caution regarding the option for issuers to use a supplementary prospectus rather than a full draw-down prospectus for issuing green bonds (and certain other additions to a class). For all issuances that concern a green bond or other sustainability-labelled bond, the prospectus should be required to include the provisions we recommend in our response to Questions 41, 42 and 43 above, including issuer-level covenants linked to transition plans, in order to guard against greenwashing and ensure that investors have the information needed to understand and evaluate the sustainability claims.

[59] PRR 3.4 UK Supplementary Prospectus

[60] Hoepner A and Schneider F, *Exit vs. Voice vs. Denial of (re)Entry*, August 2022, including at p.12: "threatening to Deny Debt when a firm is looking to refinance provides for the strongest Voice power."

Protected forward looking statements

Please consider the comments below a response to Questions 44 to 53.

We limit ourselves to general comments on the application of the PFLS criteria proposed by the FCA insofar as they concern climate, sustainability and transition plan disclosures under the new POATR regime.

As a starting point, the recklessness / dishonesty standard represents an extremely high legal and evidential barrier to liability for untrue or misleading statements or omissions. The application of the negligence standard in relation to the prospectus serves a critical purpose in that it affords a higher degree of protection to investors who purchase securities based on this central offering document than the protection afforded in relation to the release of information to the market in general. This rightly reflects the central role of the prospectus and the heavy reliance that is naturally placed on it by prospective investors in the securities of the issuer.

In that context, any decision to dilute the applicable liability standard for certain prospectus disclosures must be: (a) specifically targeted (as exceptions to the general rule); and (b) rigorously justified in the specific instance in question. As a general comment, we therefore appreciate the careful approach to PFLS eligibility and qualifying criteria outlined by the FCA In Chapter 7, including the identification of categories of information in relation to which a weakening of the liability standard would be inappropriate. In particular, we support the principle that, given the purpose of the PFLS concept being to encourage more (fulsome) disclosure, there is generally no sense in weaking the liability standard for information which it is already mandatory to disclose in the prospectus, as doing so would "*simply shift the liability treatment more favourably towards issuers for no wider benefit*."[61]

It is our strong view that the specific disclosures for 'mineral companies' that we recommend above in relation to Question 40 should remain subject to the negligence standard, on the basis that "*rigour and assurance in the production of these reports, which liability helps to discipline, is an important safeguard against over-optimistic assumptions*."[62]

As regards our concerns that the eligibility of mandatory climate and transition plan disclosures as PFLS should be: (a) as targeted as possible; and (b) specifically justified, in order to avoid compromising the accountability necessary to guarantee the reliability and usefulness of these disclosures, please see our response to Question 36, above. Those comments apply equally to transition plan disclosures and the broader climate-related disclosures proposed by the FCA.

[61] See paragraph 22 of Engagement Paper 3. Similar logic is adopted in CP24/12.
[62] The FCA's own words from para. 30 of Engagement Paper 3: Engagement Paper 3: Protected forward-looking statements (fca.org.uk).