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Mobilising IOSCO to take action on the TCFD recommendations

State of play in relation to TCFD implementation

Institutional investors managing over $80 trillion in assets have publicly committed to support the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD) since its launch in 2017. However, there is significant concern that momentum on TCFD implementation is an EU phenomenon, with other economies much slower on the uptake, resulting in regulatory divergence on climate risk disclosure and the build-up of systemic risks in key sectors of the global economy. This regulatory divergence makes it difficult for investors with a global portfolio to accurately assess risk and allocate capital across global portfolios.

The usefulness of climate reporting depends on wider harmonisation and standardisation across different jurisdictions. Widespread adoption of the TCFD recommendations across the global capital markets would help protect investors by providing information that is highly relevant to investment decision-making, thereby enabling them to allocate capital efficiently and at the same time reduce systemic financial risk. It would also help address the fact that reporting companies often have to respond to a web of overlapping climate risk reporting frameworks, creating inconsistency both within and across jurisdictions.

What can IOSCO do?

Recognised as the global standard setter for securities markets, the International Organisation of Securities Commissions (IOSCO) is well positioned to play a key role in harmonising climate risk reporting and promoting widespread implementation of the TCFD recommendations across the global capital markets. IOSCO's reach as an organisation is expansive: its 217 members are responsible for regulating over 95% of the world's securities markets.

IOSCO has different ways in which to promote harmonised climate risk reporting and implementation of the TCFD recommendations:

- As a first step, IOSCO could issue a formal acknowledgement of the TCFD recommendations and announce any steps it plans to take with regard to climate risk disclosure.
- The IOSCO Methodology and the IOSCO Principles could be updated to expressly refer to climate risk and promote the TCFD recommendations as a means of addressing it.
- IOSCO could develop new TCFD-based climate risk reporting standards that can be used by its members in performing their regulatory functions. To start, IOSCO could help clarify the meaning of 'materiality' with respect to prospective climate-related contingencies and provide guidance on how such assessments should be performed.
- IOSCO could produce reports on climate risk drawing upon the work initiated by the TCFD. These could, for instance, outline the process by which its members could incorporate the TCFD recommendations into their existing regulatory frameworks, offer guidance on principles of scenario analysis, or on how preparers should assess the materiality of potential future climate-related financial impacts.

NB. IOSCO has no regulatory powers and it would not be mandating TCFD-based disclosure. By acknowledging the TCFD recommendations and initiating work on climate-related financial disclosure, IOSCO can help national regulators understand how to integrate the TCFD recommendations into existing corporate governance, reporting frameworks or listing requirements, and achieve consistency in global regulatory approaches.

What can investors do?

As a membership organisation - with membership being comprised chiefly of national securities regulators - investors wanting to engage with IOSCO on harmonised climate risk disclosure and implementation of the TCFD recommendations have two options:

1. Engage their national securities regulator and request that the regulator use its position as an IOSCO member to influence the organisation. For instance, investors could ask the national regulator representative to push for Committee 1 to work towards one of the outputs identified in this briefing.

2. Engage IOSCO directly, for example, by requesting the Chair of Committee 1 to undertake one of the activities outlined above to incorporate the TCFD recommendations into an existing IOSCO work stream or to develop a new work stream on climate risk reporting more generally.

IOSCO's role in addressing climate related financial risk:

IOSCO itself has no regulatory power or legal authority to enforce its standards or recommendations. Its power as an organisation lies in its ability to influence the activities and policies of national and regional securities regulators and thereby achieve consistency in global regulatory approaches. Action by IOSCO could have a 'trickle-down effect' of national regulators integrating the TCFD recommendations into existing corporate governance and reporting frameworks (whether by 'soft law' corporate governance and stewardship codes or via mandatory listing requirements).

The Committee on Issuer Accounting, Audit and Disclosure (Committee 1) is most relevant to harmonised climate risk reporting and the TCFD recommendations. It is responsible for monitoring key international developments related to disclosure and enhancing the quality and transparency of the information that investors receive from listed companies.

IOSCO's key regulatory standards are the IOSCO Objectives and Principles of Securities Regulation (the IOSCO Principles). These are based on three objectives: protecting investors; ensuring that markets are fair, efficient and transparent; and reducing systemic risk. It has stated that it is a 'top priority' for members to achieve the effective implementation of the IOSCO Principles in order to protect investors and mitigate against global systemic risk.

In the context of climate risk, two IOSCO Principles are particularly relevant:

- IOSCO Principle 6 (focused on regulators): The Regulator should have or contribute to a process to identify, monitor, mitigate and manage systemic risk, appropriate to its mandate.
- IOSCO Principle 16 (focused at issuers): There should be full, accurate and timely disclosure of financial results, risk and other information which is material to investors' decisions.

Climate change is widely regarded as a systemic risk. It is also a material risk for many of the world's largest public companies, from fossil fuel producers and power utilities to banks, asset managers and insurers.

Implementation of the TCFD recommendations by IOSCO regulator members would help fulfil IOSCO Principles 6 and 16 through contributing to a process to identify, monitor, mitigate and manage a systemic risk, and through ensuring that issuers provide full, accurate and timely disclosure of climate related information that is material to investors' decisions.

Why do investors care?

Including IOSCO engagement in the suite of investor stewardship activities will be particularly important for investors with portfolios spanning multiple jurisdictions.

One motivating factor for investors to engage national securities regulators or IOSCO directly is the overall impact of climate-related financial risks on portfolios e.g. the systemic risk that unabated climate change may have upon all investments through lower growth rates or climate-driven losses. However, materiality determinations are typically left to management and the board and these may choose to exclude a probing analysis from their disclosures if they deem climate impacts unlikely or immaterial.

This is where IOSCO member regulators have a role to play to ensure more transparent and efficient capital markets through better and harmonised climate risk disclosure. For investors, communicating the importance of these concerns to IOSCO and its member regulators is a key step to ensuring they have the right information to assess risk and allocate capital accordingly.