

The emerging global framework for climate change regulation Keynote address at City Week 2021

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Today I will concentrate on one topic—climate—and what I believe to be the critical factors needed to ensure that climate finance has a solid foundation in regulation.

For some time, regulators have drawn attention to problems with the consistency, availability and reliability of the information needed for investors to incorporate climate into their decisions. This goes hand-in-hand with concerns about greenwashing.

More recently, there has been a substantial increase in the amount of publicly-available climate-related corporate information, standards and ratings. This has made it even harder to make sense of what has become another form of information overload.

The good news is that we are now seeing meaningful progress in efforts by regulators to help make sense of so much noise in the system.

The Network of Central Banks and Supervisors for Greening the Financial System was an early mover, issuing guidance for supervisors to consider climate and environmental risks lurking in banking and insurer balance sheets.

And only a few days ago, the G7 was the latest organisation to recognise the urgent need for a globally-consistent corporate reporting standard for sustainability. Its communique explicitly supported the important move by the IFRS¹ Foundation to establish a new Sustainability Standards Board to achieve this.

Of special significance to this vital IFRS project is the initiative by the major private-sector sustainability standard setters², with the Task Force on Climate-related Financial Disclosures (TCFD), to work with the IFRS Foundation on a prototype for what is likely to be the first globally-harmonised corporate climate reporting standard.

And at the International Organization of Securities Commissions (IOSCO), whose Board I chair, we are now fully engaged with the IFRS Foundation on the establishment of its new Sustainability Standards Board.

Note: This is the text of the speech as drafted, which may differ from the delivered version.

¹ International Financial Reporting Standards.

² The Climate Disclosure Standards Board, Global Reporting Initiative, International Integrated Reporting Council, Sustainability Accounting Standards Board and CDP (formerly the Carbon Disclosure Project).

So sustainable finance is now a clear IOSCO priority. And in addition to an imminent—and important—IOSCO report on corporate-level disclosures, we will shortly publish reports on environmental, social and governance (ESG) ratings as well as regulatory expectations for asset managers. I will briefly touch on each of these projects in turn.

IFRS Foundation proposal

Our most urgent task at the moment is to fully engage with the IFRS Foundation's efforts to develop a global baseline standard for corporate sustainability reporting.

In my view, this effort is essential to enable companies worldwide to clearly communicate how sustainability factors relate to their financials.

The initial focus will be on climate, for two main reasons.

First, the impact of climate change on the environment and society is now blindingly obvious, as is the fact that the time available to take action is rapidly running out.

Second, climate is an area which is already rich in science-based data and widely-adopted disclosure frameworks—not least through the great work done by TCFD.

In essence, the IFRS Foundation's project promises to synthesise and develop the leading international disclosure frameworks into a single global standard. This should enable the data and metrics of most relevance to an individual company's *enterprise value* to be reported in a consistent, comparable and useful manner.

I am convinced that this concept of enterprise value is the right initial approach, especially as it correlates with the more conventional remit of market regulators by focussing on information of most relevance to the providers of capital.

An enterprise value approach starts with reporting on the financial risks of climate change to a business. But it also extends to how a company's own activities have an impact on the environment and society, because this can also be of material relevance to value.

The resulting standard should therefore increasingly cross-over to the "double materiality" concept that is a core feature of the European Union's (EU) plans for sustainability disclosures.

At a recent IOSCO board meeting, we heard firm support for the IFRS initiative, although the timeline is quite ambitious.

I should explain why IOSCO's sustainability work is so heavily intertwined with this project.

First, we chair the IFRS Foundation's Monitoring Board, which already oversees the public interest dimension of the Foundation's work.

This is part of a three-tier governance structure—together with trustees and a standard-setting board—now used in the production of international accounting standards.

The basic idea is that this tried-and-trusted governance framework will be expanded and adapted as the basis for governance of the new Sustainability Standards Board.

On top of this, IOSCO has proposed that a multi-stakeholder consultative committee should be set up to ensure that the IFRS standards are fully interoperable with jurisdiction-level standards, whether in the EU, the US or elsewhere.

In addition, technical working groups have been set up within IFRS as well as in IOSCO. The IFRS group is developing the prototype climate reporting standard I mentioned earlier. And the IOSCO group will assess this emerging standard with a view to potential endorsement for use across its extremely large membership.

The IOSCO evaluation will of course be rigorous, as it has been in relation to IOSCO's past endorsement of IFRS accounting standards.

The current aim is for the new Sustainability Standards Board to be set up by COP26³ and climate standards to be issued as early as mid-2022.

To sum up, we are looking to IFRS to deliver a sophisticated baseline climate reporting standard, building on the TCFD framework, which can then be adopted and mandated across jurisdictions.

This standard should be fit for investor needs and provide a basis for the development of credible, independent sustainability audits. It will evolve dynamically and in time also embrace sustainability topics in addition to climate.

We fully recognise that individual jurisdictions will introduce their own sustainability disclosure requirements. But we need to ensure that the overall effort delivers the level of global consistency and comparability that investors desperately need.

ESG data and ratings

The second area IOSCO is focussed on relates to ESG data providers and ESG rating services.

This is a big challenge given that most jurisdictions do not have regulatory frameworks which explicitly cover these activities.

Many on the buy and sell sides have signalled how confusing the multiplicity of different ESG ratings choices can be, once again raising serious questions about relevance, reliability and greenwashing. So we are now working on ways to ensure better transparency and clearer definitions.

Our work is likely to involve guidance to service providers and rating agencies, together with recommendations for regulators on how to deal with potential conflicts of interest. We expect to publish our report on data providers and ratings by mid-July.

Asset management industry

The third major area of focus for IOSCO is to encourage the global fund management industry to incorporate more meaningful climate-related considerations into its investment and risk management processes.

³ The UK will host the 26th UN Climate Change Conference of the Parties (COP26) in Glasgow from 31 October to 12 November 2021.

Asset managers are at the heart of the investment chain and improving their practices relating to climate and other sustainability-related risks is critical to enable quality information to be provided to end-investors.

And with corporate disclosures progressing towards globally-consistent sustainability reporting, managers should have even stronger incentives to consider how best to integrate sustainability factors into their investment strategies.

Here we are again building on the TCFD recommendations to set out a credible and consistent framework which fund managers can use to improve sustainability-related practices and disclosures.

Importantly, this will explicitly address the risk of greenwashing, ensuring that communications with investors include reliable and proportionate information.

Investors should then be able to gain a far better understanding of the emissions they finance and how climate risks can affect their portfolios. They should also have better tools to enable them to hold asset managers to account for their public commitments to sustainability goals.

Conclusion

I want to conclude by saying that we are at a pivotal moment for all of the projects I have described. The next few months will be critical.

The IFRS global baseline project is particularly crucial. At the same time, the EU is developing its own set of standards and the US is also working on climate disclosure standards under the new administration.

Within IOSCO, we fully accept that jurisdictional-level approaches are bound to differ. But for corporate reporting, it is essential that these domestic approaches will be fully interoperable with the emerging global baseline, avoiding the rule conflicts or overlaps that could devalue the overall effort.

We cannot work in jurisdictional silos when the climate emergency does not respect national boundaries. It is absolutely essential that we resist fragmentation, which is a real risk all regulators are very aware of.

Capital markets are far better than banks at funding the significant private-sector innovations needed to achieve net-zero goals. So close global collaboration and coordination is essential to enable private finance to be fully engaged in support of the transition to net-zero.

Of course, pathways to achieve a maximum 1.5°C temperature increase and net-zero ambitions will hinge on a wide range of government policies and related incentives. First and foremost is the need to establish a meaningful price on carbon.

But the corporate reporting and other disclosure-focussed projects I have described are also essential. They will provide investors with the information they need to align their decisions with the evolution of climate policy and innovation at, and beyond, COP26.

Thank you.