31 July 2021

General Manager, Policy Development
Policy and Advice Division
Australian Prudential Regulation Authority

Via email: PolicyDevelopment@apra.gov.au

Draft APRA Prudential Practice Guide CPG 229: Climate Change Financial Risks

The Financial Services Council (FSC) welcomes the opportunity to provide comment on the draft APRA Prudential Practice Guide CPG 229: Climate Change Financial Risks.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks and licensed trustee companies. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing $3 trillion on behalf of more than 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange and is the fourth largest pool of managed funds in the world.

The FSC supports the release of this draft practice guide. The FSC believes it is important that financial institutions consider climate risk as a real financial risk. It is also important that Australian financial services regulators send a clear signal to regulated entities that climate risks should be disclosed in alignment with the Task Force on Climate-related Financial Disclosures (TCFD).

Currently, no existing specific legal requirements exist to report on climate risk, although we note that current broader obligations contain within their scope the reporting of climate risk, such as sections 299A(1) and 1013D(1)(l) of the *Corporations Act 2001*, Reg 7.9.14C of the *Corporations Regulations* and APRA RG 288.

However, we believe APRA and other Australian regulators should be taking steps toward mandatory minimum reporting requirements that align with the TCFD. This would align Australia with major trading partners that have introduced such requirements or are actively considering it, such as the European Union, Hong Kong, New Zealand, Switzerland, the United Kingdom and the United States. This would help to provide the financial services industry with greater certainty as to their obligations in reporting and managing climate risk.

Any move toward mandatory requirements should be introduced in a coordinated way with other regulators and with government, to ensure that consistent requirements apply to listed companies

Financial Services Council Ltd
Level 5, 16 Spring Street
Sydney NSW 2000

E. info@fsc.org.au
W. fsc.org.au
ABN 82 080 744 163

@FinServCouncil
@FinServCouncil
@financial-services-council

and other public reporting entitles, not just APRA-regulated institutions.

As the draft guidance recognises, climate risk disclosure is a rapidly evolving topic in many jurisdictions around the world, especially in light of widespread net-zero commitments by many governments and companies. In this regard, the FSC encourages APRA to keep monitoring best practice developments in other major markets and updating its guidance as necessary. It would also greatly help industry and provide further clarity if APRA provided a guide roadmap with timeframes to implement disclosures.

We make the following specific recommendations about the draft guidance:

1. We would welcome further guidance in the following areas:
    a. Governance (para 13-17):
        i. We recommend including guidance on the disclosure of the link between climate-related performance and executive remuneration including clarity as to what good climate related performance involves.
        ii. The reference to 'senior staff' (para 17) could be broadened to 'relevant staff' so that training and capacity building in the management of climate risks cascades across the organisation.
    b. Risk Monitoring (para 30): We recommend further guidance on the sorts of circumstances that might trigger a review of a company's risk management policies and procedures, including the sorts of triggers that relate to risk data and metrics.
    c. Scenario analysis (para 36-44): We recommend that the guidance covers the following:
        i. Uncertainty around use of scenarios is not a reason to fail to undertake scenario analysis.
        ii. Entities should where possible use credible scenarios from commonly referenced sources to promote comparability and standardisation. Where a bespoke scenario is used, entities should disclose the underlying assumptions and how this deviates from standard assumptions used by commonly referenced scenarios.
        iii. In relation to the future temperature rise scenarios used (para 40(b)), the guidance recommends including a scenario of 2 degrees or less. APRA should ensure the guidance keeps up to date with current science and global developments, such as whether 1.5 degrees vs 2 degrees of warming should be used as a minimum.
        iv. The development and undertaking of scenario analysis can be a significant cost for funds. Clarification from APRA would be welcome as to the extent of scenario analysis expected of entities so that unnecessary costs aren't incurred by superannuation members. We would be happy to engage with APRA on what might be acceptable for certain sized funds.
        v. Case study examples would be helpful.
    d. Best financial interests duty: We would welcome clarity in the practice guide that consideration of climate risk in investment decisions does not conflict with the new

best financial interests duty. The FSC and our members agree that considering ESG factors is an important aspect of long-term investing, and there is clear evidence that incorporating ESG considerations into investment decisions has led to stronger long-term financial performance over most asset classes and most investment horizons. However, clear guidance from APRA would be welcome so that the duty is not used to discourage trustee engagement with climate risk issues.

2. APRA should give consideration to ensuring expectations are aligned in the practice guide and SPG530 Investment Governance, in particular the relevant environmental and social governance sections 34-36. Further clarity would be welcome on criteria for considering ESG factors in formulating the investment strategy, and expectations for excluding investments or positively weighting non-financial factors as a result of ESG considerations.
    i. SPG 530 states that APRA expects an RSE licensee would be able to demonstrate appropriate analysis to support the formulation of an investment strategy that has an ESG focus (such as climate risk), and ensure it satisfies the best (financial) interests of beneficiaries and satisfies liquidity and diversity requirements under section 52 of the SIS Act. Clarification in the practice guide would be welcome on APRA's expectations as to level of required quantitative and qualitative analysis required in analysing risk and undertaking scenario analysis in order to meet the threshold of demonstrating appropriate analysis.

3. We support keeping the guidance at a high enough level to allow financial services firms and industry flexibility to develop their risk reporting and management in an area where best practice is constantly developing. For instance, flexibility is important for smaller asset managers to be able to work with APRA regulated entities in developing an appropriate approach to reporting. While maintaining its high-level nature, the guidance should seek to address specific sectors as much as possible, accounting for differences in approach taken by banks, insurers and superannuation trustees. This would help provide consistency within these sectors.
    a. For instance, the practice guide could provide more specific guidance under Risk Management on how APRA expects a prudent RSE licensee would consider the management of climate risk in areas like investment strategies for the fund as a whole or specific asset classes.

If you wish to follow up on this submission or have any questions, please contact Chaneg Torres, Policy Manager at ctorres@fsc.org.au.

Kind regards,

Chaneg Torres
Policy Manager
Investments & Global Markets