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Impak Finance answer to CSA's climate-related disclosures consultation

We are participating in this consultation in our quality of extra-financial rating agency[1] based in Montreal with experience of analyzing and scoring environmental and social data of issuers, including climate change. Please find below our answers in blue to the questions we deem relevant to our knowledge of issuers and climate disclosure.

Experience with TCFD recommendations

1. For reporting issuers that have provided climate-related disclosures voluntarily in accordance with the TCFD recommendations, what has been the experience generally in providing those disclosures?

As a rating agency, we look into climate related disclosures of issuers. If the objective of this regulation is for investors to limit their financial risks regarding consequences of climate change on issuers' assets, TCFD helps give insight into that. On the other hand, if the objective is to provide information on issuers that are best avoiding or minimizing their own impact on climate change, then TCFD is insufficient as it only addresses the issue of climate change from a financial materiality's perspective (or shareholders' perspective).

It is important to note that focusing only on how the company is financially impacted by climate change defies the purpose of ensuring future returns as it is a short term vision. In the long run, sustainable companies (i.e. more adapted to climate change and impacting less the environment), perform better financially.

If we circle back to the question, in our experience of analyzing and scoring issuers, we notice that issuers using only TCFD to report on climate are usually not the most sustainable players overall (acting best to avoid harm done to the environment and society).

Disclosure of GHG Emissions and Scenario Analysis

2. For reporting issuers, do you currently disclose GHG emissions on a voluntary basis? If so, are the GHG emissions calculated in accordance with the GHG Protocol.

Issuers not subject to specific regulation most often use the GHG Protocol, although loosely as not all guidelines are followed. For example, justification for not providing scope 3 emissions is often lacking.

Some companies use sector-specific standards which are more relevant and meaningful than generic initiatives.

3. For reporting issuers, do you currently conduct climate scenario analysis (regardless of whether the analysis is disclosed)? If so, what are the benefits and challenges with preparing and/or disclosing the analysis?

From our perspective as a rating agency, most quoted companies which report according to the TCFD conduct climate scenario analysis and present the results. However a climate scenario analysis is an expensive and/or time consuming process, which can be a challenge for ventures or smaller companies. Additionally, investors are not equally interested in climate scenario analysis or have the expertise to apply it appropriately. Finally, there are some criteria that can indicate the level of urgency the company faces concerning climate change impacts. Not all sectors are equally or simultaneously impacted by climate change

[1] https://www.impakfinance.com/

events. Therefore, requiring a climate scenario analysis from companies a certain size or more quickly impacted would solve some of these issues. Mapping the reliance of the company on climate-impacted products is part of a climate scenario analysis and would be an important first step.

4. Under the Draft Regulation, scenario analysis would not be required. Is this approach appropriate? Should the Draft Regulation require this disclosure? Should issuers have the option to not provide this disclosure and explain why they have not done so?
We recommend that the Draft Regulation starts by requiring scenario analysis at least for companies above a certain threshold or in certain sectors, in order to set the tone. Bigger companies (in terms of revenues or number of employees) or those impacting more - or more impacted by - climate change are required to provide a scenario analysis.

5. The TCFD recommendations contemplate disclosure of GHG emissions, where such information is material. • The Draft Regulation contemplates issuers having the option to disclose GHG emissions or explain why they have not done so. Is this approach appropriate? Materiality is key for avoiding cherry-picking and greenwashing. We would recommend following the GHG protocol, which only allows for not disclosing scope 3, providing a strong justification for it, scope 1 and 2 being the minimum disclosure.

• As an alternative, the CSA is consulting on requiring issuers to disclose Scope 1 GHG emissions. Is this approach appropriate? Should disclosure of Scope 1 GHG emissions only be required where such information is material?
This approach appears to be subjective as there are few companies nowadays for which GHG emissions are not material, particularly in the range of companies potentially targeted by the CSA. Scope 1 might not be the most material scope for all companies - see next bullet point. Also, GHG protocol started recommending disclosure of at least scope 1 and 2 emissions two decades ago (GHG protocol, 2001).

• Should disclosure of Scope 2 GHG emissions and Scope 3 GHG emissions be mandatory?
As early as 2001, the GHG protocol described the 3 scopes and how to report on them. Depending on the sector a company is in, one scope could be more important than the other. This is why we consider it essential for companies to report at least scope 1 and 2. For manufacturing companies, scope 2 can be much more important than scope 1, and both scopes allow for a portrayal of the operational emissions of the company. The GHG protocol recommends a reporting of scope 3 but leaves to corporations the choice of which categories to report but to justify this choice.

• For those issuers who are already required to report GHG emissions under existing federal or provincial legislation, would the requirement in the Draft Regulation to include GHG emissions in the issuer's AIF or annual MD&A (if an issuer elects to disclose these emissions) present a timing challenge given the respective filing deadlines? If so, what is the best way to address this timing challenge? We do not have a particular comment except that we recommend the most punctual reporting.

6. The Draft Regulation contemplates that issuers that provide GHG disclosures would be required to use a GHG emissions reporting standard in measuring their GHG emissions, being the GHG Protocol or a reporting standard comparable with the GHG Protocol (as

described in the Draft Policy Statement). Further, where an issuer uses a reporting standard that is not the GHG Protocol, it would be required to disclose how the reporting standard used is comparable with the GHG Protocol. • As issuers have the option of providing GHG disclosures, should a specific reporting standard, such as the GHG Protocol, be mandated when such disclosures are provided? • Is the GHG Protocol appropriate for all reporting issuers? Should issuers be given the flexibility to use alternative reporting standards that are comparable with the GHG Protocol? • Are there other reporting standards that address the disclosure needs of users or the different circumstances of issuers across multiple industries and should they be specifically identified as suitable methodologies?

7. The Draft Regulation does not require the GHG emissions to be audited. Should there be a requirement for some form of assurance on GHG emissions reporting?
Sustainability regulations move towards assurance as it is the only way to ensure good quality data and transparency. In our view, assurance is the highest level of evidence an issuer can provide.

8. The Draft Regulation permits an issuer to incorporate GHG disclosure by reference to another document. Is this appropriate? Should this be expanded to include other disclosure requirements of the Draft Regulation? Our position would be to limit the number of documents as climate governance and climate change risk management are closely related to other risk management topics and it would be counterproductive to separate them from both the issuer's and the reader's perspective.

Usefulness and benefits of disclosures contemplated by the Draft Regulation

9. What climate-related information is most important for investors' investment and voting decisions? How is this information incorporated into these decisions? Is there additional information that investors require?
In our view, investors would benefit from the broadest, most comprehensive climate-related disclosure, including emissions data and detailed information regarding issuers' management of climate-related risks. The next 30 years will see an increase of average temperatures ranging anywhere from between 1.5 to 5 °C, with severe, unprecedented socioeconomic impacts that will likely present themselves in a non-linear fashion (McKinsey, 2020). In response to these impacts, issuers in most sectors will face a rapidly changing regulatory stance. Market behaviours are also bound to evolve in similar, unpredictable ways.

Investors who wish to limit their exposure to these risks will require the most complete set of information, without limitation by a materiality analysis which will always be anchored in present considerations and subject to a high level of discretion on behalf of issuers (Condon *et al,* 2021). The evaluation of issuers' exposure to climate-related risks (both physical and transition) therefore requires, at the very least, that information regarding their Scope 1 and 2 emissions, and their risk assessment and management strategies, be available. Hence, regulators should require the utmost level of transparency from issuers on these matters, where possible.

10. What are the anticipated benefits associated with providing the disclosures contemplated by the Draft Regulation? How would the Draft Regulation enhance the current level of

climate-related disclosures provided by reporting issuers in Canada?
We do not see that the requirements contemplated by the Draft Regulation, or any other climate-related disclosure requirement that could be implemented by the CSA, would significantly hinder capital markets activity in Canada. Despite growing requirements regarding climate and overall ESG-themed disclosure around the world, 2021 has seen very high levels of IPO activity in all markets including Europe, where environmental disclosure requirements are more stringent then in Canada (EY, 2021).

Furthermore, scientific evidence reports that climate-related, and more broadly ESG-themed disclosure reduce information asymmetries (Felini & Raimondo, 2021; Adhikari & Zhou, 2021) and that such disclosure is of great use to investment professionals in their decision-making process (CFA Institute, 2019)

Costs and challenges of disclosures contemplated by the Draft Regulation

11. What are the anticipated costs and challenges associated with providing the disclosures contemplated by the Draft Regulation?

12. Do the costs and challenges vary among the four core TCFD recommendations related to governance, strategy, risk management, and metrics and targets? For example, are some of the disclosures more (or less) challenging to prepare?

13. The costs of obtaining and presenting new disclosures may be proportionally greater for venture issuers that may have scarce resources. Would more accommodations for venture issuers be needed? If so, what accommodations would address these concerns while still balancing the reasonable information needs of investors? Alternatively, should venture issuers be exempted from some or all of the requirements of the Draft Regulation?

We acknowledge that venture issuers face specific challenges regarding the cost of disclosure, and that this cost should not unduly hinder their ability to adequately raise capital. A differentiated approach, including, inter alia, disclosure exemptions might be pertinent to alleviate this burden if based on the already existing regime for venture issuers.

However, we note that many venture issuers operate in high-emitting or potentially high-emitting industries, including sectors related to energy and natural resources. Hence, a sector-based approach might be warranted to tailor these exemptions while providing investors with data when such data is relevant.

Guidance on disclosure requirements

14. We have provided guidance in the Draft Policy Statement on the disclosure required by the Draft Regulation. Are there any other tools, guidance or data sources that would be helpful in preparing these disclosures that the Draft Policy Statement should refer to?

15. Does the guidance set out in the Draft Policy Statement sufficiently explain the interaction of the risk disclosure requirement in the Draft Regulation with the existing risk disclosure requirements in Regulation 51-102?

Prospectus Disclosure

16. Form 41-101F1 Information Required in a Prospectus does not contain the climate-related disclosure requirements contemplated by the Draft Regulation. Should an issuer be required to include the disclosure required by the Draft Regulation in a long form prospectus? If so, at what point during the phased-in implementation of the Draft Regulation should these disclosure requirements apply in the context of a long form prospectus?
We consider that information that is material to investors one year after an issuer's IPO was most likely material at the moment of the IPO. In our view, mandating climate-related disclosure in the long-form prospectus is a necessary complement to the Draft Regulation.

This is already applicable to governance matters (including Board gender diversity), through the inclusion of Form 58-101F1 in Form 41-101F1. We do not see any reason to adopt a different approach in the case of climate-related disclosure.

Phased-in implementation
17. The Draft Regulation contemplates a phased-in transition of the disclosure requirements, with non-venture issuers subject to a one-year transition phase and venture issuers subject to a three-year transition phase. Assuming the Draft Regulation comes into force December 31, 2022 and the issuer has a December 31 year-end, these disclosures would be included in annual filings due in 2024 and 2026 for non-venture issuers and venture issuers, respectively. • Would the transition provisions in the Draft Regulation provide reporting issuers with sufficient time to review the Draft Regulation and prepare and file the required disclosures? • Does the phased-in implementation based on non-venture or venture status address the concerns, if any, regarding the challenges and costs associated with providing the disclosures contemplated by the Draft Regulation, particularly for venture issuers? If not, how could these concerns be addressed?

Future ESG considerations
18. In its comment letter to the IFRS Foundation's consultation paper published in September 2020, the CSA stated that developing a global set of sustainability reporting standards for climate related information is an appropriate starting point, with broader environmental factors and other sustainability topics to be considered in the future. What broader sustainability or ESG topics should be prioritized for the future?

We recommend to focus first on climate change with a complete perspective, i.e. double materiality not only from a financial perspective, such as TCFD.

Beyond climate change, hierarchizing other environmental or social topics would be questionable as most topics are interrelated. That is also the European Commission's position as after having published a first version of the European taxonomy focused on climate change, the other environmental topics to be published simultaneously are Circular economy, Biodiversity, Water resources, Pollution, while other working groups are working on the Social taxonomy, expected soon after (subject being more complex).

Biodiversity is gaining traction since the detailed results of IPBES research review pointing at unprecedented collapse (IPBES, 2019) and since then, the link between climate change, biodiversity and the pandemic being made.

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