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February 5, 2019

Dear Members of the Expert Panel on Sustainable Finance,

Re: CPA Canada Response to the Interim Report of the Expert Panel on Sustainable Finance

Chartered Professional Accountants of Canada (CPA Canada) appreciates the opportunity to respond to the Interim Report of the Expert Panel on Sustainable Finance (the Expert Panel).

We agree that a successful transition to a low-carbon economy will require the engagement of mainstream financial markets. We also agree that concerted efforts and commitment by all parties are required to address the lack of momentum in sustainable finance in Canada to date. The work of the Expert Panel is an excellent step in that direction.

About CPA Canada

CPA Canada is one of the largest national accounting organizations in the world, representing more than 210,000 members. CPA Canada conducts research into current and emerging business issues and supports the setting of accounting, auditing and assurance standards for business, not-for-profit organizations and government. CPA Canada also issues guidance and thought leadership on a variety of technical matters, publishes professional literature and develops education and professional certification programs.

CPA Canada has been researching and writing on the business issues related to climate change for over 20 years, focusing on issues of governance, accounting, auditing and corporate disclosures. Most recently, CPA Canada, with funding support from Natural Resources Canada, is:

- conducting research with Canadian institutional investors, among others, about how best to provide decision-useful climate-related financial disclosures aligned with the Task Force on Climate-related Financial Disclosure (TCFD) recommendations
- developing a training program for directors, executives and CPAs to address climate-related financial matters within the private sector
- working with selected municipalities to understand how the TCFD recommendations could be adapted and utilized by cities
- planning a follow-up study on climate-related financial disclosures by Canadian public companies and progress in adopting the TCFD recommendations.

In 2017, CPA Canada published an initial State of Play report on climate-related financial disclosures by Canadian public companies.¹ This study indicated an opportunity to increase transparency around climate risk through enhanced disclosures, thereby improving the ability of investors and other stakeholders to price risk and allocate capital efficiently during the transition to a low-carbon economy. It highlighted some considerations for public companies and regulators, offering several questions for which answers might enhance climate-related disclosures.

Role of CPAs in the Sustainable Finance Ecosystem

As the Interim Report acknowledges, the transition to a low-carbon economy will require a knowledgeable financial ecosystem. The engagement of CPAs is crucial to support financial decision-making, given their pivotal role in understanding and managing systemic risks and opportunities, financial and accounting systems and standards, effective internal and external disclosures and governance.

Key Findings

In formulating our response to the Interim Report, we have drawn on our knowledge of risk and strategic management, governance, and corporate reporting practices and challenges. We solicited the input of strategic advisors to CPA Canada and our extensive network of volunteers representing small, medium and large issuers, investors, and auditors.

In December 2018, CPA Canada hosted a roundtable in Toronto to provide an opportunity for stakeholders to share their views on opportunities and challenges relating to sustainable finance and climate-related risk disclosures, and how to promote low-carbon, clean economic growth in Canada.

In addition to representatives from the Expert Panel and CPA Canada, CPAs and business leaders from a range of sectors and diverse backgrounds, including finance and accounting, audit and assurance, risk management, institutional investment, governance and boards of directors participated in the roundtable.

Roundtable participants concentrated their input primarily on two foundational elements set out in the Expert Panel's Interim Report:

- ✓ 3.3 effective climate-related financial disclosures
- ✓ 3.5 a knowledgeable financial support ecosystem.

The following are some key themes that have emerged from the roundtable discussion and our research and outreach to date:

1) Improved Communication

A national communication plan should be developed to educate the public about the opportunities and risks of climate change adaptation. In addition, businesses will benefit from a better understanding of the business case concerning the opportunities and risks that climate change presents.

2) Decision-Useful Information

The market needs reliable, decision-useful information about severe weather events to be able to assess the physical risks climate change presents for corporations, investors and governments.

3) Materiality

There is an expectations gap between what investors consider material climate-related financial information and what corporations believe to be most useful and relevant disclosures to investors.

¹ <https://www.cpacanada.ca/en/business-and-accounting-resources/financial-and-non-financial-reporting/sustainability-environmental-and-social-reporting/publications/climate-related-disclosure-study>

Further research needs to be undertaken in this area and companies will benefit from additional guidance on how to assess materiality of climate-related issues.

4) Accounting and Auditing Implications

Additional guidance is needed to understand how climate-related issues are factored into the application of accounting standards, the preparation of financial statements and the audit of those financial statements.

5) Lead by Example

Governments can lead by example in decision-making and reporting by encouraging crown corporations to implement the TCFD recommendations, modified as necessary for public sector reporting. Municipalities could benefit from continued financial assistance from the federal government to encourage sharing of best practices in the integration of climate considerations into cross-functional planning, decision-making and operational processes.

6) Increased Canadian Participation in Global Initiatives

It is important that key Canadian stakeholders participate in relevant global climate change business initiatives to ensure the perspective of the Canadian economy is effectively communicated.

7) Education and Training

There is consensus that more targeted education and training is required for professionals and business and government leaders to build capacity for the transition to a low-carbon economy.

We elaborate on the preceding themes and provide recommendations for the Expert Panel's consideration in the Appendix to this letter.

CPA Canada supports the important work of the Expert Panel on Sustainable Finance and appreciates the opportunity to offer comments on its Interim Report.

Should you have any questions on our research and comments, please contact Rosemary McGuire, Director, Research, Guidance and Support (rmcguire@cpacanada.ca).

Yours truly,



Gordon Beal, CPA, CA, M.Ed.

Vice President, Research, Guidance and Support

Chartered Professional Accountants of Canada

Appendix – Detailed Recommendations for Expert Panel Consideration

1. Improved Communication

i) Climate change adaptation education plan

Extreme weather is already costing Canadians a great deal and will only cost more the longer Canada ignores the need for related significant infrastructure upgrades and investments. While apparent to the Expert Panel and others, many members of the public may not be as familiar with this concept.

We heard from roundtable participants that it would be constructive if there were a national communication plan that would:

- educate taxpayers and other members of the public on the costs and opportunities of climate change adaptation in the hope of providing improved policy certainty and more widespread support for policies that address adaptation
- provide a definition of sustainable finance that would be easily relatable and would focus on opportunities, not only on the negative aspects of climate change.

With a more certain government policy that spans beyond four-year election periods, governments and organizations can more effectively and efficiently allocate capital resources for inevitable climate-change adaptation.

ii) Make the business case to managements and boards that climate change presents business opportunities as well as risks

We heard that businesses need a clear link between providing increased disclosure of climate-related financial information and value to the company and its shareholders.

The following might assist in providing a business case for improved climate-change disclosures:

- research and case studies clearly demonstrating, across industry sectors, the business value in incorporating climate-change adaptation and mitigation issues into an organization's risk assessment, strategic planning and disclosure systems
- research by industry associations or others setting out best climate-related financial-disclosure practices of peer companies in their industries not only in Canada but particularly in other countries where climate-related financial disclosures tend to be more robust.

Part of the business case for companies is that improved disclosures may attract and retain long-term investors. Institutional investors are increasingly reporting to their beneficiaries/clients using the TCFD recommendations. To be able to report, they are seeking better disclosures from organizations in which they invest. In CPA Canada's recent research², every institutional investor interviewed purchases climate-related financial data on companies from third-party data providers, usually because companies themselves have not provided adequate decision-useful information on climate-related matters. These third-party providers have no obligation to provide a balanced assessment and

² As part of CPA Canada's climate change disclosure and decision-making project with support from Natural Resources Canada, we conducted interviews with institutional investors with assets under management totaling approximately \$1.9 trillion, as well as a bond rating agency and a third-party data provider. The focus of these interviews was to understand how investors use climate-related information and what information they use in decision-making processes.

may or may not have instituted appropriate internal controls and processes to ensure reliability and accuracy of information.

We note that the federal government is collaborating with institutional investors who invest globally, including the Caisse de dépôt et placement du Québec and Ontario Teachers' Pension Plan, to advance comprehensive climate change reporting and sustainable infrastructure investing.³ We have heard that effective ways to focus corporations on improved climate-related reporting are to include:

- ✓ questions about climate-related financial information in engagement meetings and on analyst earnings calls
- ✓ climate-related financial information in mainstream sell-side analyst reports.

2. Decision-Useful Information

- i) *Linking of weather and infrastructure data to enable more effective capital investment, business resilience and disaster continuity planning*

Based on our research, few companies and investors disclose the risks and opportunities related to key infrastructure that could be impacted by severe weather events, including floods, ice storms, wildfires and melting ice. Infrastructure impacts can directly and indirectly impact the businesses that rely on that infrastructure.

While there are initiatives that attempt to show how climate change will impact specific geographical areas, there is a need to link geographical weather information to specific physical asset and infrastructure locations.⁴ This applies to company-owned facilities in Canada and globally and their supply chains, to government departments that invest in public infrastructure and to investment portfolios holding these assets.

The federal government should continue to play an important role in facilitating collaboration among governments, insurance companies, corporations, industry associations and others to develop an accessible, decision-useful database of weather and climate information.

3. Materiality

- i) *Further guidance on materiality*

Securities regulators currently mandate disclosure of material information, including climate-related financial information.⁵ However, as securities regulators state, there is no bright-line test for materiality. Determining materiality requires judgment.

³ <https://www.newswire.ca/news-releases/leading-canadian-and-g7-investors-come-together-in-support-of-global-development-initiatives-684685981.html>

⁴ e.g., Climate Atlas <https://climateatlas.ca/>; WRI Aqueduct Tool <https://www.wri.org/our-work/project/aqueduct>; Swiss Re CatNet <https://www.swissre.com/reinsurance/property-and-casualty/solutions/property-specialty-solutions/catnet.html>; Canadian Centre for Climate Services <https://www.canada.ca/en/environment-climate-change/news/2018/04/canadian-centre-for-climate-services.html>

⁵ CSA Staff Notice 51-333 Environmental Reporting Guidance October 27, 2010 https://www.osc.gov.on.ca/documents/en/Securities-Category5/csa_20101027_51-333_environmental-reporting.pdf; and CSA Staff Notice 51-354 Report on Climate change related Disclosure Project April 5, 2018 https://www.osc.gov.on.ca/documents/en/Securities-Category5/csa_20180405_climate-change-related-disclosure-project.pdf

When companies were queried about why they had not disclosed climate-related information, they often stated that they did not consider the matter material.

Institutional investors, on the other hand, expressed the view that their default position was that climate-related financial information was material for every company unless otherwise stated. In research currently being undertaken by CPA Canada, investors noted they are often not able to determine whether the company had appropriately assessed key elements of climate-related financial information and concluded they were not material or the company had not properly assessed the matter.

Based on interviews conducted by CPA Canada, there is consensus among institutional investors that all companies should provide disclosure about their governance of climate-related financial information and their high-level risk assessment of climate-related financial information, whether companies deem this information material or not. This is consistent with the TCFD recommendations.

Roundtable participants suggested the Canadian Securities Administrators (CSA) should amend its governance policy to require disclosure of governance over climate change issues.

As provinces have jurisdiction over securities regulation, we acknowledge that it would take collaboration among provincial regulators to mandate disclosures about governance and risk assessment of climate-related financial information across Canada. It is doubtful that every jurisdiction would favour mandatory disclosures at this time, possibly due to the additional regulatory burden that some might perceive as attaching to this.

There may be insights to assessing materiality by analyzing how institutional investors do so. For example, we have heard that most institutional investors start with the Sustainability Accounting Standards Board (SASB) Materiality Map, adjusting the map as necessary based on discussions with portfolio managers. Investors also use industry-specific guidance, Global Reporting Initiative (GRI) standards, Carbon Disclosure Project (CDP) survey responses and international peer reporting to assist in identifying material issues.

The federal government could play an important role by encouraging and funding further research on practical materiality guidance for key Canadian industrial sectors.

4) Accounting and Auditing Implications

i) Better understand the accounting and auditing implications of climate-related matters.

Climate change has the potential to impact the valuation of an organization's assets and liabilities. For example, we heard that more frequent and severe weather should impact the estimate of the longevity of infrastructure and lead to revised depreciation rates and increased operating and maintenance costs over the asset's life. In addition, we heard that some assets, including real estate, may need to be accounted for as stranded assets, particularly if such assets are no longer eligible for insurance coverage.

Several accounting and auditing standards may require consideration of climate-related matters including those related to fair value measurements, impairment assessments, asset retirement obligations, contingent liabilities, use of specialists, and materiality assessments. The standards make no specific mention of climate change, however.

Similar to what the CSA undertook in CSA Staff Notice 51-333 *Environmental Reporting Guidance*⁶ we heard it would be helpful if standard setters developed guidance on how climate-related issues

⁶ https://www.osc.gov.on.ca/documents/en/Securities-Category5/csa_20101027_51-333_environmental-reporting.pdf

should be evaluated in the application of existing accounting and assurance standards. We also heard that it would be helpful if case studies were developed demonstrating the potential impact of climate-related risks on the value of assets and liabilities within an organization.

5) Lead by Example

i) Federal government to lead by example

To set an appropriate example, we heard suggestions that the federal government could demonstrate leadership in a number of areas, including requiring:

- Crown Corporations to disclose appropriate climate-related financial data in their annual filings, including whether considered material or not, information on their governance and risk assessment related to climate-related financial matters. When deemed material, further climate-related financial disclosures should be provided, consistent with the TCFD recommendations, adapted as necessary.
- pension plans controlled by the federal government to adopt the TCFD recommendations.

In addition, we heard support for the federal government's investments in the retrofitting of existing infrastructure in the private and public sectors.⁷ To the extent feasible, infrastructure retrofitting or new building funded in part or in whole by federal funds should incorporate best available technologies and building code requirements to build climate resilience.

ii) Municipal governments and best practices in climate change integration

As part of CPA Canada's current initiative with Natural Resources Canada, a working group has been established to create guidance for municipalities on assessing the maturity of the integration of climate-change considerations into decision-making processes and external reporting. This project will showcase how three leading Canadian municipalities are factoring climate-related financial information into their decision-making and aligning with the TCFD recommendations.

We heard support for continuing federal government funding/financial assistance to encourage and enable best climate change practices throughout municipalities in Canada. This support has been echoed in CPA Canada's work with municipalities on the topic of TCFD and integration of climate change information into decision-making.

6) Increased Canadian Participation in Global Initiatives

i) Fund participation in relevant global initiatives

Canadians already participate in selected global initiatives concerning aspects of the transition to a low-carbon economy. But such participation takes resources – time, money and commitment.

We heard that, given the nature of the Canadian economy, it is important to encourage more Canadian representation in key global initiatives related to climate change issues. Examples of these initiatives include the World Economic Forum, the UNFCCC⁸ Conference of the Parties and UNEP FI⁹ projects. It would be helpful for the federal government to fund those industry associations, member

⁷ E.g., <https://www.cbc.ca/news/canada/london/london-ontario-west-5-federal-funding-1.4988175>

⁸ United Nations Framework Convention on Climate Change (<https://unfccc.int/>)

⁹ <https://www.unepfi.org/>

organizations and qualified individuals prepared to devote intellectual capital and time to actively contribute to global initiatives on climate-related financial issues.

7) Education and Training

- i) Continue to expand the funding of relevant education and training programs to build professional capacity for key participants in the public and private sectors*

While leading boards of directors and executives understand the business issues involved in climate-related financial matters, public sector leaders could also benefit from more training on the relevance and importance of these issues. In response, CPA Canada, with funding from Natural Resources Canada, is currently developing climate change training programs for directors, executives and CPAs to build professional capacity.

We heard that, despite efforts to date, there is a critical need for more education and training among professionals to build capacity. In addition to existing programs, we continue to support the federal government's funding of relevant climate change education and training. We heard widespread support for ongoing and targeted education and training programs for professionals within the necessary knowledge ecosystem (e.g. CPAs, engineers, lawyers, urban planners).