Brussels, 31 January 2019

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EBF answers to the Report on climate-related disclosures by the Technical Expert Group on Sustainable Finance

Question 1. Do you have any comments on Chapter 2 "Disclosures under the Directive: Principles and Rationale for Non-Financial Reporting" of the report?

Answer 1.

In the first place, we would like to welcome the revision of the non-binding guidelines of the Non-Financial Reporting Directive (NFRD) to provide further guidance on how to disclose climate-related information.

The Technical Expert Group (TEG) Report is a key step in the much-needed transition to a low-carbon economy.

We see a need for consistency. In addition to the guidance on climate-related disclosures, we would like to see further work on Sector specific Guidance for banks and other financial entities in addition to the guidance on climate-related disclosures.

Due to the specific and strict regulatory framework for risk disclosures by banks, it is key for the banking sector to avoid that any specific criteria regarding climate-related disclosures could trigger disclosures of climate-related information that might be presented as non-consistent with mandatory financial information disclosed under other regulatory requirements (e.g., risk disclosures required under Pillar 3). These considerations are critical in order not to compromise the credibility and effectiveness of the current risk-based prudential network in the EU.

The primary focus of the climate-related disclosure for banks should identify the most relevant KPIs/ESG factors linked to national and international climate-related policies and other strategic components of banks' strategies to achieve specific climate-related goals with sufficient materiality to the banking activities. As mentioned in the Report, climate-related opportunities, such as green financing will themselves, in many cases, act as risk mitigation measures.

Without disregarding the obligation to disclose impacts of the bank's operations on the environment, as stated in the NFRD, given the uncertainty surrounding the ongoing work in terms of the climate-related Taxonomy, we consider that banks climate-related disclosures should be developed, at least in the beginning, as a qualitative and distinctive forward-looking information tool regarding climate-related endeavours and achievements,

gradually towards a quantitative approach (proportional to the size of the financial institution). Once developed, this approach would be completed with a comply or explain procedure.

Q2. Do you have any comments on Chapter 3 "Alignment of NFRD and TCFD" of the report?

A2.

The level of alignment between both NFRD and TCFD frameworks is satisfactory. However, disclosure of climate-related risks by banks requires further assessment of the outcome of the work on the climate-related disclosures framework and criteria within the overall regulatory requirements regarding banks' risk disclosures.

Once the current regulatory uncertainty regarding sustainability issues (taxonomy of sustainable activities, mandatory ESG disclosures by investment firms, benchmarks, credit rating agencies) is addressed, financial and non-financial information regarding climate-related transition and physical risks should be integrated.

Q3. Do you have any comments on Chapter 4.1 "Business Model" of the report?

A3.

Criteria for Type 1 information disclosure (of mandatory nature) should be flexible enough to provide banks with enough room to self-assess the effects of climate-related issues on their business model.

Regarding type 2 and 3 information, the disclosure (of discretionary nature) must be focused on the identification of opportunities and resilience capacity of banks regarding climate-related impacts over the business model.

We would welcome further clarifications regarding the perception that, as it stands now, the disclosures under "Other Disclosure (Type 3)", may prove less demanding than the disclosures required under "Supplementary Disclosure (Type 2)".

Q4. Do you have any comments on Chapter 4.2 "Policies and Due Diligence Processes" of the report?

A4.

Disclosure regarding Policies and Due Diligence must be focused on information regarding the efforts and specific actions taken by banks to adopt governance and risk management procedures suitable to identify, measure, mitigate and manage not only climate-related risks, but also opportunities.

More than a pure disclosure of climate-related specific risks and opportunities to which banks are exposed, disclosure at this level must highlight and identify bank's capacity to gradually integrate climate-related issues in the culture of the organization, with effective governance and proper board oversight and engagement, internal control and risk management, risk internal classification framework, compliance plan and day-to-day action, internal expertise and technical resources allocation and investment.

We don't see relevant differences between first point on type 2 "explain the roles of the various (board) committees" and the disclosure type 3 proposed. We would propose to maintain it in type 2 and take it out of type 3.

Q5. Do you have any comments on Chapter 4.3 "Outcomes" of the report?

A5.

The disclosure of information related to how the asset portfolio, products and services are impacted by climate change can prove to be a challenge, because of a present structural lack of reliable data. Furthermore, it may imply to make public some additional information that is commercially sensitive, hence exposing sensitive strategy to competition.

Q6. Do you have any comments on Chapter 4.4 "Principal Risks and Their Management" of the report?

A6.

Considering that specific climate-related risks and associated disclosures are facing significant developments - for example, the technical criteria for determining the environmental sustainability of an economic activity in line with the environmental objectives of the Taxonomy regulation proposal is yet to be defined – the future presentation of "consistent and historical disclosures", using a backward-looking approach may be difficult. We therefore ask to not include the word "historical" in the update of the EU Commission's voluntary guidelines on non-financial disclosures.

Q7. Do you have any comments on Chapter 4.5.1 "General and Supplementary KPIs" of the report?

A7.

The provision of scope 3 information - all indirect emissions which are not included in Scope 2 along a value chain, both upstream with suppliers and downstream with clients – will be challenging. We should be aware that this will depend on further disclosure, at least, by corporate clients on their own GHG emissions. Given the recognized lack of available robust methodologies with market consensus, as stated in the report, we urge for further developments in this area, as to foster the comparability and completeness of such information and improve the reach of financial intermediation activities in disclosing information regarding Scope 3 GHG emissions.

While the reporting of quantitative information of banks that adopted the TCFD recommendations is very low, especially due to the lack of objective data, banks are committed to improve data quality, and are working on different methodologies to create meaningful accounting of climate impacts with the industries they finance.

Other alternative solutions should be considered to report about climate impacts through banking activities instead of GHG accounting scope 3 a(p 39). There are already new methodologies under development (e.g. 2dii, PCAF…) focusing on sector specific metrics/targets that are being disclosed by counterparties and used in climate scenarios, so they can provide an overview of the alignment of banks' activities portfolios with the Paris Agreement. This forward-looking sector-based approach could be used for the most carbon sensitive sectors and can be more useful that scope 3 GHG emissions absolute

numbers when engaging counterparties around their transition. It can be also seen as a risk mitigation for banks.

Primary data on supply chain impacts is often poor, although it is expected to improve when data requirements start to be generally included in third party contracts and service level agreements.

Engaging with customers to gather information on their climate impacts will also prove challenging, until they are compulsorily requested by the regulators. However, since part of the impact will depend on the provision of products and services of the company itself (and the bank's capital allocation decisions, in the case of credit institutions), the development of new products and services or climate-related incentives and contractual conditionality, will contribute to the disclosure of relevant KPIs.

Q8. Do you have any comments on Chapter 4.5.2 "Sectoral and Company-specific KPIs: Non-financial Companies" of the report?

A8.

Q9. Do you have any comments on Chapter 5 "Sector specific Guidance: Banks and Insurance Undertakings" of the report?

A9.

5.2

Further work and guidance on best practices on disclosure format and methodology regarding the "concise risk statement" (p. 34) would be useful, due to its relevance to ensure consistency between climate-related disclosures and other banks' general risk reporting and disclosure procedures.

We disagree with the statement that "Financial institutions should consider disclosing climate-related incentives in risk and commercial teams" (p. 34). We understand that this kind of disclosure should not be considered, in order not to compromise the credibility and effectiveness of the risk management function of the risk team, and to prevent the creation of a "sustainable bubble".

As we already stated in our position on the Regulation on disclosures relating to sustainable investments and sustainability risks, to use remuneration policies as a mechanism to encourage sustainable investments could be detrimental to the correct functioning of credit institutions and the correct sustainability analysis done by the professionals involved in these assessments. Remuneration policies are already regulated in the prudential package, in MiFID, and EBA guidelines, so we do not agree with their inclusion in other regulatory proposals which can also give raise to inconsistencies.

The development of further guidance regarding disclosures on banks "integration of climate-related risks and opportunities of their prospective investment opportunities" and "sustainable finance considerations in suitability assessments of customers' preferences and awareness" (p. 34) would be welcomed and must be dully considered in the future work on the specific climate-related disclosures in the banking sector.

5.4

Regarding the guidance on "Principal Risks and Their Management" we consider that some clarification and consistency must be added to the Type 1 disclosures regarding ESG

factors incorporation and their influence over "financial risk position" and "credit analysis" in order to avoid inconsistency or misleading information overlap between climate-related risk factors and other CRD IV Pillar 3 general risk disclosure by banks. It would be worth to evaluate the merit of work on further guidance and principle-based approach promoting additional criteria for bank specific climate-related disclosures of risk and opportunities aligned and consistent with the CRD IV Pillar 3 general risk disclosure.

In our view, this approach would be useful to ensure that climate-related disclosures by banks will be used as an effective and qualitative set of useful information to allow all the relevant stakeholders to obtain a more depth and critical information to properly assess the climate-related factors, risks and opportunities with significant materiality (in the sense of the Point 3.1. of the NBGs on NFRD) to the overall and prospective assessment of the climate-related impact over the general risk level and appetite disclosed by banks under CRD IV Pillar 3 requirements.

In any case, the definition of financial materiality thresholds for climate related risks and the disclosure of current and potential impact of climate-related risks on credit and market risk exposure are delicate matters that require time to be implemented and need to be tested.

Climate-related disclosures must complement and strengthen the CRD IV Pillar 3 requirements and further work on climate-related disclosures for the banking sector must follow this overarching outcome.

Since, as the Report recognizes, banks should focus on indirect climate impacts, despite the well-known challenges associated with it, often on a "best effort basis", the disclosure of the "classification of carbon-related assets and investments", of "changes in loan estimates under different climate-related scenarios" (p. 35) will be extremely challenging.

We would also like to signal some issues regarding the amount of collateral highly exposed to climate-related risks (p. 36). In terms of consistency, while we encourage to keep track of the data banks have available and are accountable for, the reporting of this kind of data could pose an issue of wider sustainability and reputational risks though diminish the positive effects companies' transition to more sustainable activities.

5.5

Furthermore, the effort on the widening of Scope 3 emissions reporting is a challenge that requires, as also somewhat suggested in the document, robust methodologies, that are currently lacking.

As mentioned in A7 above, other alternative solutions should be considered to report about climate impacts through the banking activities instead of GHG accounting scope 3.

5.6

There should be considered that even if the EC guidelines are voluntary, in some jurisdictions they are considered by the Supervisory Authority during the NSF compliance assessment, therefore, there is the risk that the updated guidelines (June 2019) might represent a binding reference for NFS already from 2020 in some jurisdictions. This would not provide enough time for reporters to apply the guidelines in an extensive manner.

5.7

Regarding "stress testing" and "scenario analysis" mentioned as KPIs type 2, we think both should consider physical risks and transition risks. Now it is proposed to focus stress testing on physical risks and scenario analysis on transition risks

Q10. Do you have any additional comments on the report as a whole?

A10.

As stated in the first answers, we welcome the revision of the non-binding guidelines of the NFRD to provide further guidance on how to disclose climate-related information.

In addition to the guidance on climate-related disclosures, we would like to see further work on Sector specific Guidance for banks and other financial entities, considering the specificities of the core activity of credit institutions as well as the sector-specific regulatory framework regarding risk disclosures.

Banks are, per definition, financial intermediaries, and even within the climate-related issues, they act more as intermediaries of risks than as elements of risks. We can see that when trying to compile the numbers regarding GHG emissions, an assessing the difference between the total Scope 1 and 2 emissions and the estimated (and for sure incomplete) Scope 3 emissions. As such, it should be given an increased focus on further guidance to overcome the lack of available data on clients, rather than just encourage in the innovation of such reporting (Scope 3 GHG emissions). We would like to reiterate our comments in A7 and on A8 5.5 above, that other alternative solutions should be considered to report about climate impacts through banking activities instead of GHG accounting scope 3.Not all companies or credit institutions have access to the same type of data. Therefore, to improve the level of disclosures and to minimize costs it is important to promote open access and open source data. The more the information is in the public domain and the same approach is used by all, the less costly its implementation and the less ambiguous the interpretation.

KPIs proposed for banks need to have tagged assets highly exposed to transition risks and physical risks what will require investment and resources on IT platform and data.

Furthermore, we should also be aware of the need for proportionality, on this type of disclosures even keeping in mind the selected range of entities captured in the scope of the NFRD and the different type of disclosure (type 1, 2 and 3). Small banks, without the range of resources and tools of larger banks, or even banks that might want to develop further their disclosure but don’t have yet the necessary expertise, must be supported with further guidance. The principle of materiality should also be applied to these banks and to the requirements to small companies both regarding disclosure and information to banks.

The alignment of a possible future revision of the NFRD with the banking sector needs and specificities must be ensured through future work on regulatory integration of ESG factors, both in terms of organizational requirements (management, control, audit, compliance, etc.) and in strategic options concerning the business model (for example regarding core business activities, services and products, costumer-relation management and centricity).

As banks it would be useful to summarize all metrics considered (type 1, 2 and 3) in a single table or annex on the document.

Finally, the TEG report refers not only to the non-binding guidelines of the EU Commission, but also to the overarching binding NFRD. We assume that the revision of the regulations for the reporting of non-financial information after only one reporting period is premature and therefore cannot deliver well-founded results.