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Creating a climate of change digest

The International Sustainability Standards Board (ISSB) requests information on its Consultation on Agenda Priorities

Leading off

The ISSB is seeking feedback on a proposed agenda that would inform a two-year work plan, implemented between 2024 and 2026. The two-year time frame is abbreviated in comparison to other standard setting consultations to provide the ISSB latitude to address emerging risk and allow for novel research opportunities.[1]

Four research projects are part of the ISSB's key priorities. Three of the four projects focus on matters related to sustainability, including (1) biodiversity, ecosystems, and ecosystem services (BEES); (2) human capital; and (3) human rights.[2] The goals of these projects are similarly described in the proposed work plan and generally address:

- Establishment of frameworks for definitions and categories of subtopics and issues considering business and sustainability-related disclosures.
- Assessment of risks, opportunities, and significant investor information for identified subtopics.
- Inventory of the current range of practices, tools, and standards used to quantify and report on sustainability information.

The ISSB's fourth project on reporting integration will leverage previous work on IFRS® S1 and IFRS S2. It will set forth guidance outlining further incorporation of sustainability-related financial data with other data sources and develop a comprehensive disclosure framework for corporate reporting.[3]

The ISSB is requesting feedback via email or online survey by September 1, 2023. The request for information covers eight core questions, four of which are specific to the approach for the main research projects. The remaining four questions focus on the ISSB's strategic direction and activities, work plan inclusion criteria, new projects, and other comments. During the fourth quarter of 2023 and the first quarter of 2024, the ISSB plans to conduct a review of the feedback and issue a summary statement outlining the nature of the comments received and the finalized workplan. As mentioned above, the workplan would be executed starting in 2024 and should be effective for two years.

Oregon restricts use of wildfire risk maps by insurers

Oregon Governor Tina Kotek has signed a consumer protection law that would prevent insurers from cancelling or not renewing a homeowner's insurance policy—or increasing the premium—based on a statewide map of wildfire risk.[4]

The bill, Senate Bill 82 (SB 82), includes amendments that homeowners' rates "shall not be excessive, inadequate, or unfairly discriminatory" but states that no homeowner's premium rate shall be deemed inadequate unless this rate is "unreasonably low for the insurance" to the point where its "continued use endangers the solvency of the insurer."[5]

The legislation would also give a policyholder the time to repair, rebuild, or replace damaged or lost property. Specifically, the bill would allow the insured at least a year after the date of the insurer's initial payment toward the cash value of the property that was damaged or lost or at least two years if the damage or loss happened in a location that was subject to a declaration of a state of emergency or other official proclamation. Companies must also provide additional living expenses to the insured, subject to the policy limits, for two years after the date of the damage or loss to the insured's primary dwelling if the damage or loss occurred in a location that was subject to a declaration of a state of emergency and the damage or loss is directly related to the emergency that was the subject of the declaration.[6]

The Financial Stability Board's (FSB) Compensation Monitoring Contact Group (CMCG) report takes a closer look at climate-related financial risk factors in compensation frameworks across financial services.

The CMCG's report is primarily based on information collected from a survey taken between April 2022 and June 2022, which inquired about survey participants' current practices (2020–2021) and future developments (2022–2023). Additional perspectives were also gathered from a September 2022 workshop for senior banking, insurance, and asset management executives, consultants, and academics.[7]

The report discusses the importance of climate change in the financial sector, its presence as a priority from both regulatory and organization standpoints, and how organizations are trending toward incorporating climate-related metrics into compensation frameworks. More broadly, the report mentions several jurisdictions that are monitoring how these metrics are being woven into compensation frameworks across the financial services industry. The report reflects that all efforts, whether organization specific or industry specific, are in their infancy and are characterized by a range of challenges,[8] including:

- **Data.** "The lack of reliable data makes it difficult to implement climate risk strategies, to make climate risk decisions as well as to conduct climate risk analysis."
- **Key performance indicators (KPIs).** "It is difficult to develop objectively measurable KPIs that are acceptable to all stakeholders."
- **Misalignment of timing.** "The challenge is the setting of short-term climate goals on an annual basis as is required in a compensation framework, while the external commitments tend to have much longer time frames, and progress is non-linear."
- **Incentivization across the organization.** "There is some difficulty in incorporating climate and sustainability aspects as part of the daily operations of a financial institution."

Some examples of climate-related metrics that have commonly been incorporated in compensation frameworks include "the reduction of carbon footprint, provision of sustainable finance and products, and accountability type measures such as leadership in the climate-related area."[9] In addition, the report suggests that entities have also conducted peer benchmarking activities using external metrics for comparison purposes.

So far, these metrics have reportedly not had a significant impact on the compensation of executives or senior management given their relative level of consideration. However, the report notes that this could change in the future as firms place additional emphasis on the metrics as core elements in the compensation function.

InnSure is selected to deploy grants as part of a $6.5 million insurance sector award to spur New York's innovation and transformation climate initiatives for businesses and consumers.

New York State is moving forcefully toward its objective to meet outstanding climate goals, which include reducing greenhouse gas emissions by 85% by the year 2050. A $6.5 million award is expected to help spur innovation and research on the development of new insurance solutions that will help the industry access and use technologies to develop climate-conscious insurance products to benefit consumers and the marketplace.[10] The program was announced in September 2022 to make sure that the insurance sector keeps apace of new innovations and technology.[11]

New York Governor Kathy Hochul announced this spring that the nonprofit InnSure is the recipient of the program administrator award to deploy the grants. InnSure will be awarded up to $1.5 million to work with managing general underwriters and agents who will research, develop, and evaluate new insurance products and policies. The nonprofit will then award up to $5 million in competitive grants, which are anticipated to be announced later in 2023.

InnSure will work with the New York State Energy Research and Development Authority (NYSERDA) to co-develop a competitive program granting awards to insurance innovators they believe can improve access to data and revolutionize insurance coverage for climate tech businesses and consumers.

"Removing barriers to innovative climate technologies that lower carbon emissions is a critical part of reaching New York's ambitious climate goals," Governor Hochul said. "By supporting new insurance policies for New Yorkers purchasing cutting-edge, climate-friendly products, we can offer protection and reassurance for consumers and companies alike to help ensure our state continues to lead in climate innovation."[12]

New York's $6 billion Clean Energy Fund, established in 2016 and modified in 2021, supplies funding for this project.[13] In general, NYSERDA's innovation program, which supports innovation and technology to promote the state's climate equity and decarbonization goals, is sending $800 million into investments in the climate and innovation space over 10 years through grants and commercialization support.[14]

The comprehensive climate goals for New York State also include a mandate that at least 35% to 40% of the benefits of clean energy investments are directed to disadvantaged communities.

A staff report from the Federal Reserve Bank of New York investigates US banks' exposures to climate transition risks and finds that the US banks have meaningful but manageable exposures to transition risks.[15]

The report investigates US banks' exposures to alternative policies and scenarios targeted at promoting the transition to a low-carbon economy. The report leverages insights from academic literature that has estimated sectoral effects of climate transition policies on the US economy.

Key findings from the report are as follows:[16]

1. Exposures vary by model and policy scenario with the largest estimates coming from the NGFS [Network for Greening the Financial System] (2022a) disorderly transition scenario,[17] where the average bank exposure reaches 9% as of 2022.
2. Exposures increase with the stringency of a carbon tax policy but tend to benefit from a corporate or capital tax cut redistribution policy relative to a lump-sum dividend.
3. In the assumption that loans to industries in the top two deciles most affected by the transition policy lose their entire value, banks' exposures would increase 12% to 14%.
4. There is a downward trend in banks' exposures to the riskiest industries consistent with a gradual reduction in the funding to these industries.
5. Effects of more stringent policies on banks' exposures to transition risks are strongest for high-emitting banks.

The findings suggest that US banks' exposures to transition risks are no higher than 16% of their loan portfolio even in the most severe scenario, which assumes loans to the top two deciles of the industries most affected by the transition lose their entire value.[18] This research could potentially be used to inform the development of assumptions used in climate-related scenario analysis.

The ISSB provides a reprieve for IFRS S1 and S2 implementation

In early April, the ISSB decided to assist companies with the shift to IFRS S1 by allowing them to report only on climate-related risks and opportunities in the first year they apply IFRS S1 and IFRS S2 and to begin reporting on their other sustainability-related risks and opportunities in the second year.[19] The ISSB's actions were taken to address market feedback that the organization should prioritize the development of climate standards while not limiting their work to climate-related information.

The ISSB's relief package would exempt companies from the following obligations in the first year they use the ISSB Standards.[20]

- "Provide disclosures about sustainability-related risks and opportunities beyond climate-related information;
- Provide annual sustainability-related disclosures at the same time as the related financial statements;
- Provide comparative information;
- Disclose Scope 3 greenhouse gas emissions; and
- Use the Green House Gas Protocol to measure emissions, if they are currently using a different approach."

Taken together, this combination of exemptions may likely provide substantial relief to the applicable companies while allowing them to direct focus toward other foundational aspects of preparedness (e.g., systems design and implementation, reporting capacity). It is noted that this one-year transition relief would not change the effective date of IFRS S1 and would not have any implications on the application of or requirements in IFRS S2. IFRS S1 would remain effective for annual reporting periods beginning on or after January 1, 2024. However, the requirements in IFRS S1 would apply only insofar as they relate to the disclosure of climate-related financial information.[21]

Emmanuel Faber, Chair of the ISSB, stated, "This transitional relief ensures companies can phase in their approach, initially focusing on the quality of the climate-related information they provide."

The IFRS S1 and S2 will be released toward the end of the second quarter of 2023.[22]

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Additional Deloitte US perspective on climate risks

For additional insights, please see our ongoing series on how climate risks are shaping US financial regulatory initiatives and the impact these developments may have on the financial services industry and the broader economy:

- Deloitte 2022 *CxO Sustainability Report*
- 2023 financial services industry outlooks
- Ingraining sustainability in the next era of ESG investing
- The CIO's call to action: Driving an environmentally sustainable tech agenda to accelerate organizational change
- Climate Change and Financial Risk Digest | Deloitte US
- Center for Regulatory Strategy - Sustainability, climate & equity | Deloitte US

Endnotes

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