ESG Standard Brief

Task Force on Climate Related Financial Disclosures (TCFD)

The Task Force on Climate Related Financial Disclosures (TCFD) is a framework for translating the physical and transition risks of climate change to financial outcomes. It makes recommendations across four categories: governance, strategy, risk management, and metrics & targets. It can be useful for understanding how climate change will affect environmental impact outputs and outcomes; it is not useful for specific social impact considerations.

https://www.fsb-tcfd.org/

THE BASICS

TCFD is a voluntary framework for disclosing financial impacts from climate change.

TCFD divides climate-related risks into two categories – risks related to the ***transition*** to a lower-carbon economy, and ***physical*** risks from the impact of climate change.[1] The framework guides the user to establish or utilize climate scenario analysis,[2] disclose governance, strategy, risk management, and metrics & targets risks across these scenarios, and helps translate these disclosures into financial risks that will impact the business.[3]

Core Elements of Recommended Climate-Related Financial Disclosures

Governance
The organization's governance around climate-related risks and opportunities

Strategy
The actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning

Risk Management
The processes used by the organization to identify, assess, and manage climate-related risks

Metrics and Targets
The metrics and targets used to assess and manage relevant climate-related risks and opportunities

Source: The Task Force on Climate-Related Financial Disclosures. Accessed 3/14/2022.

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USEFUL FOR

Financial and non-financial institutions across public and private sectors. Although the TCFD was originally created for private sector financial institutions, it has quickly been adapted to cover non-financial companies across the private and public sectors. In 2020, a total of 1,069 financial institutions responsible for $194 trillion in assets had made disclosures under TCFD.[4]

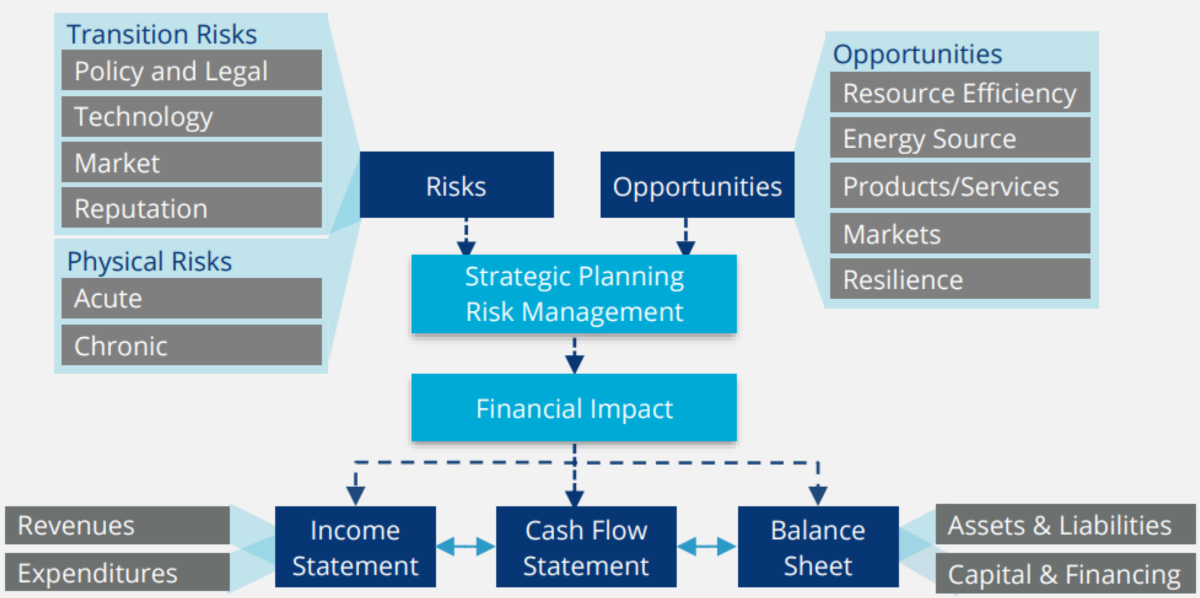
Companies driving environmental action. Companies that make disclosures are driving environmental action through the process of using data to inform effective environmental risks and strategies. The collective of disclosure data is being used to track environmental progress across markets and industries, and to provide accountability where needed.[5]

IMPLEMENTATION & IMPACT

Translating disclosures to financial impacts. The flowchart below provides a high-level overview of how companies' disclosures will translate to their financials.

Mandatory or voluntary? It's evolving. As of 2021, financial regulators, central banks, and governments have begun to rapidly adopt ranges of voluntary to mandatory TCFD disclosure. New Zealand became the first country to introduce mandatory TCFD disclosure for financial institutions; Canada has tied pandemic bailout funding to TCFD disclosures; In March 2021, the

Climate-Related Risks, Opportunities, and Financial Impact



Source: The Task Force on Climate-Related Financial Disclosures. Accessed 3/14/2022.

United States SEC asked for public comment about climate disclosure, with the Treasury Secretary signaling her backing for TCFD.[6]

Resources for Implementation. TCFD maintains an online knowledge hub that serves as a walkthrough for making disclosures.[7] Several publications exist, including[8]:

- The original 2017 Recommendations
- An overview booklet / introductory material
- Guidance on scenario analysis, risk management integration, and disclosure
- Annual status reports
- A 2021 Annex to the original recommendations

Roadmap for understanding and financially integrating impact risk. TCFD recommendations cover the spectrum of ESG risk management to maximizing impact solutions. TCFD is not a negative screen for environmental investments, but rather acts as a roadmap for understanding and financially integrating the physical and transition risks that climate change may have on an impact investment.

Impact organizations can incorporate climate scenario analysis into their strategy and modify their impact metrics and targets accordingly. Further, they will be able to better measure and articulate the *how much, contribution,* and *risk* dimensions of impact.

Impact investors (capital sources and channels) who are measuring environmental outputs and/or outcomes can utilize TCFD to better understand the risks associated with climate-related impact funds. They can incorporate TCFD recommendations into their investment thesis, sourcing, and screening procedures.

CURRENT GAPS

Climate resilience strategies not yet tied to financial implications. Despite the large number of firms making climate-related disclosures, there are still a large number that struggle to communicate the financial implications of these risks. This is not a simple exercise; firms need to utilize climate scenario analysis to assess climate risk, integrate these findings into risk management, then adapt their climate resilience strategies and overall governance – and then quantitatively show how these steps achieved or avoided financial outcomes.[9]

Social risks and outcomes not incorporated. TCFD covers environmental impacts through the lens of climate change but does not explicitly make recommendations for social equity or impacts. Many agree that climate change is a social equity issue as much as it is an environmental issue, and the TCFD could add social equity to its list of areas for future work.[10] There have been calls to action from the Climate Disclosure Standards Board to utilize the TCFD framework as a foundation for social disclosure, which currently does not exist.[11] Similarly, UK pension funds and financial bodies have also called for a "TCFD of Social Risks" as regulators have continued to increase the amounts of required data disclosed around social issues.[12]

[1] https://www.tcfdhub.org/introduction/
[2] https://assets.bbhub.io/company/sites/60/2020/10/FINAL-TCFD-Technical-Supplement-062917.pdf
[3] https://assets.bbhub.io/company/sites/60/2021/10/FINAL-2017-TCFD-Report.pdf, page 8, Financial impacts
[4] https://www.fsb.org/2021/10/2021-status-report-task-force-on-climate-related-financial-disclosures/
[5] https://www.forbes.com/sites/forbesbusinesscouncil/2021/12/21/how-companies-can-prepare-for-mandatory-environmental-disclosure/?sh=5c41f0b26af0
[6] https://www.spglobal.com/esg/insights/companies-investors-face-new-pressure-from-compulsory-disclosure-of-climate-risk
[7] https://www.tcfdhub.org/
[8] https://www.fsb-tcfd.org/publications/
[9] https://www.greenbiz.com/article/how-implement-tcfd-recommendations-step-step-guide
[10] https://www.triplepundit.com/story/2018/tcfd-guidance-exacerbating-social-inequity/11151
[11] https://capitalmonitor.ai/factor/social/using-tcfd-as-the-foundation-for-the-social-in-esg/
[12] https://www.responsible-investor.com/articles/uk-pensions-and-financial-players-call-for-tcfd-for-social-risks

