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COP27 regulatory briefing

Stock-take of key regulatory policy developments

December 2022

COP27

Overview

The 27th session of the Conference of the Parties to the UN Framework Convention on Climate Change (COP27) was held in Sharm el-Sheikh, Egypt in November 2022. With so much being published ahead of and during the Conference, it was hard to stay abreast of the key regulatory policy developments. This short presentation takes stock.

An important area of focus for this year's Conference was on "loss and damage" – new funding arrangements and a dedicated fund to provide financial support for developing countries that are particularly vulnerable to the adverse effects of climate change. A "transitional committee" will be established to make recommendations by COP28 next year on how to operationalise this. Underpinning the sense of urgency were new findings that countries' current climate commitments, if fully implemented, would result in emission reductions by 2030 that fall drastically short of the decrease needed to limit global warming to 1.5 degrees.[1]

Alongside the main Conference agenda, various regulators and other standard-setting bodies used COP27 as an opportunity to publish policy updates. This presentation takes stock of some of the key regulatory and policy developments at the international level and in Europe in the run up to and during the Conference (between 24 October and 18 November 2022).

Key policy updates

We identified six themes from the updates. For each theme we summarise the main developments, our takeaways and further reading.

- Transition plans: The development and disclosure of **transition plans** will be a priority for firms in 2023, with newly-published guidance on plan development and disclosure requirements by the UN High-Level Expert Group, the Glasgow Financial Alliance for Net Zero and the UK's Transition Plan Taskforce.
- Product labels and disclosures: New proposals aimed at tackling greenwashing in investment management are part of rapidly-increasing regulatory action on greenwashing.
- Corporate reporting and disclosures: Reporting requirements are set to increase. The EU Corporate Sustainability Reporting Directive (CSRD) will shortly enter into force, following its agreement in the European Parliament plenary. A key challenge for large corporates will be navigating the complex disclosure landscape across jurisdictions.
- Climate risk management: Financial services firms are expected to continue to develop their capabilities in climate risk management and scenario analysis
- Nature and pollution: Increasing attention is being paid to nature risk and pollution, including significant changes provisionally ahead for the **automotive industry**. An updated Task Force for Nature-related Financial Disclosures (TNFD) framework for managing and disclosing **nature risks** is available for organisations to pilot.
- Energy and food: There were also a number of measures to support **energy and food security** and decarbonisation in the EU.

Further information

On each slide we identify which jurisdiction published the update. "Int." refers to international. Some updates apply only to financial services and are highlighted as "FS-only"; some apply more broadly to corporates; and some apply to specific industries.

If you have any further questions please contact a member of our sustainability regulatory strategy team. Details are at the end of this pack.

1. For further reflections see: 'What you need to know about COP27: Three takeaways from the latest climate talks", Deloitte, November 2022.

Transition plans

A priority for firms in 2023, with newly-published guidance on transition plan development and disclosure requirements

Int.

UN HLEG recommended disclosure of transition plans for businesses, financial institutions, cities, and regions

The UN's High-level Expert Group (HLEG) published a report on the net zero emissions commitments of non-state entities (8 Nov 2022). The report set out ten recommendations to help achieve net zero.

It recommended that non-state actors must publicly disclose comprehensive and actionable net zero transition plans. It made clear that non-state actors cannot claim to be net zero while continuing to build or invest in new fossil fuel supply. It also recommended that high integrity carbon credits in voluntary markets should be used for beyond value chain mitigation (i.e. mitigation action or investments that fall outside of a company's value chain) but cannot be counted toward a non-state actor's interim emissions reductions required by its net zero pathway.

HLEG recommended the launch of a new task force on net zero regulation that would convene a community of international regulators and experts to work together towards net zero.

UK

TPT launched a consultation on a "gold standard" for climate transition plans

The UK Transition Plan Taskforce (TPT) consulted on a Disclosure Framework, Implementation Guidance and Technical Annex, and launched a Sandbox to test implementation (8 Nov 2022). The TPT was established by HM Treasury in April 2022 to develop guidance on private sector climate transition plans applicable to the UK, but globally transferrable.

The TPT recommended that entities publish standalone transition plans at least every three years, and more often when the plan changes significantly. It also recommended that progress against the plan and material updates are reported annually as part of disclosures aligned to the Task Force on Climate-Related Financial Disclosures (TCFD) or the International Sustainability Standards Board (ISSB) requirements.

Once the TPT has finalised its work (expected in 2023), the UK FCA plans to draw on the framework to strengthen its transition plan disclosure expectations for listed companies, asset managers and regulated asset owners.

Int.

FS-only

GFANZ published key resources on transition plans

Following on from its June 2022 consultations, the Glasgow Financial Alliance for Net Zero (GFANZ) published a range of documents (1 Nov 2022):

- Towards a global baseline for net-zero transition planning
- Recommendations and guidance on financial institution net-zero transition plans
- Measuring portfolio alignment: driving enhancement, convergence, and adoption
- Actions to mobilise capital to emerging markets and developing economies

GFANZ also published a Progress Report (27 Oct 2022), which updated its position on its link to the UN Race to Zero. While GFANZ will "take note of the advice and guidance" of bodies such as Race to Zero, each alliance will have sole responsibility for its membership criteria.

Key takeaways

- The development and disclosure of transition plans are a priority for regulators who expect firms to make substantial progress in 2023.
- The TPT and GFANZ documents provide guidance to help firms with this task. For example, Financial institutions signed up to the GFANZ will need to examine how they align with GFANZ publications, while other FS firms will also find the resources useful.
- In the UK, firms should also consider whether/how to engage with the TPT consultation process and the TPT Sandbox. They should conduct a gap analysis of how aligned their transition plan, related governance and disclosures are to the TPT's expectations in advance of the FCA strengthening its rules.

Further recent reading from the ECRS

- Blog and report: Enhancing governance and culture to support the net zero transition, 13 Oct 2022.
- Joint Deloitte and Investment Association report: How Risk and Compliance functions can support the net zero transition: Investment Managers and net zero, 13 Jul 2022.

Other papers

- Net-Zero Insurance Alliance (NZIA) consulted on its first Target-Setting Protocol (31 Oct 2022).
- Net-Zero Banking Alliance (NZBA) published its first progress report (9 Nov 2022).
- International Organization of Securities Commissions (IOSCO) consulted on compliance carbon markets and published a discussion paper on voluntary carbon markets (9 Nov 2022).

Product labels and disclosures

New proposals aimed at tackling greenwashing in investment management are part of rapidly-increasing regulatory action on greenwashing

UK

FS-only

Extensive FCA product labelling and disclosure proposals to address greenwashing in the investment management sector

The UK FCA consulted on the Sustainability Disclosure Requirements (SDR) and investment labels (25 Oct 2022). The proposals are intended to improve transparency and trust in the sustainable investment market and focus on asset managers and their UK-based fund products and portfolio management services.

The proposals include rules on sustainable investment labels; terms that cannot be used in the names of funds that do not qualify for a label; a consumer facing summary disclosure; and detailed entity and product level disclosures. The FCA also proposed an "anti-greenwashing" rule that would apply to all regulated firms. The FCA intends to publish final rules and guidance by 30 June 2023.

The "anti-greenwashing" rule will apply when the final rules are published, while the other rules have varied timelines, with the earliest applying 12 months after the rules are finalised (i.e., provisionally 30 June 2024).

Int.

FS-only

IOSCO published good practices on greenwashing for asset managers and ESG rating and data providers

IOSCO published a call for action for voluntary standard setting bodies and industry associations in financial markets to promote good practices to counter the risk of greenwashing related to asset managers and ESG rating and data providers (7 Nov 2022). The good practices are voluntary and include detailed supporting guidance.

EU

FS-only

ESMA consulted on funds' names using ESG or sustainability-related terms

ESMA is seeking feedback on draft guidelines on the use, in funds' names, of ESG or sustainability-related terms (18 Nov 2022). For example, ESMA proposed that if a fund has any ESG-related words in its name, it needs to meet certain minimum quantitative thresholds of "sustainable investments" as defined under the Sustainable Finance Disclosure Regulation (SFDR).

The Consultation closes on 20 February 2023. The draft guidelines are expected to be applicable three months after the publication of translation on ESMA's website, with a six- month transitional period for funds launched prior to application date.

EU

FS-only

ESAs' Call for Evidence to understand greenwashing better

The European Supervisory Authorities (ESAs) published a Call for Evidence on identifying greenwashing practices in the EU financial sector, across banking, insurance, and financial markets (15 Nov 2022). The ESAs are due to deliver a progress report by end-May 2023 and a final report by end-May 2024 on greenwashing risks and supervisory action to address them.

EU

FS-only

ESMA included ESG disclosures as a new supervisory priority

ESMA included ESG disclosures alongside market data quality in the Union Strategic Supervisory Priorities (USSPs) (27 Oct 2022). ESMA and National Competent Authorities intend to foster greater transparency of ESG disclosures across the value chain to tackle greenwashing, as well as enhance supervision on ESG disclosures.

Key takeaways

- UK and EU investment managers should engage with the FCA and ESMA consultations; start considering how their UK-based funds align to the proposed new SDR labels; and assess the changes they would need to make to their fund names and disclosures for their UK and EU funds. They may also need to consider the interaction of the UK's SDR with the EU's SFDR.
- The FCA's SDR is still in the consultation phase. Nevertheless, all FCA-regulated firms should start thinking in particular about how they might comply with the "anti-greenwashing" rule, given it will apply when the rules are finalised (potentially 30 June 2024).

Further recent reading from the ECRS

- Blog: Sustainability Disclosure Requirements: FCA package of proposals on fund labels and disclosures raises new challenges for fund managers, 2 Dec 2022.
- Blog: Sustainability preferences: complex new EU rules require collection of clients' ESG preferences from August 2022, 25 Jul 2022.
- Report: Greenwashing risks in asset management, May 2022.

Other papers

- European Commission (EC) adopted a proposal for amendments to a SFDR Delegated Regulation, intended to ensure transparency in relation to gas and nuclear-related activities (31 Oct 2022).
- ESAs published letter notifying EC of up to a six-month delay in the delivery of the mandate (initially due 28 April 2023) to review the principal adverse impact indicators and financial product disclosures in the SFDR Delegated Regulation (26 Oct 2022).

Corporate reporting and disclosures

Corporate reporting requirements in the EU continue to develop

EU

European Parliament approved new CSRD reporting rules

The European Parliament approved the CSRD at its plenary meeting (10 Nov 2022). All large EU companies and non-EU companies with substantial EU activity will be required to disclose the impact of their activities on people and the planet and on their exposure to sustainability risks.

The Council adopted the proposal on 28 November. The Directive will now be published in the Official Journal and then enter into force. The rules will apply on a phased basis between 1 January 2024 and 2028, with the first reports published in 2025.

EU

EFRAG approved draft sustainability reporting standards

The European Financial Reporting Advisory Group (EFRAG) approved the first set of draft European Sustainability Reporting Standards to be submitted to the EC. These standards will underpin the CSRD and are still subject to editorial review before their final issuance.

Int.

IOSCO seeks maximum interoperability of disclosure standards

IOSCO outlined its regulatory priorities for sustainability disclosures (9 Nov 2022). IOSCO plans to move promptly to decide on endorsement of the ISSB's standards for climate disclosures and general requirements when they are finalised in 2023. IOSCO seeks maximum interoperability of standards and alignment between the ISSB and those jurisdictions seeking to implement their own standards.

EU

ESMA requests national enforcers focus on climate-related matters when they examine annual financial reports

ESMA published its annual Public Statement on European Common Enforcement Priorities for annual financial reports (28 Oct 2022). In IFRS financial statements, a priority is the consistency between climate-related disclosures within IFRS financial statements and non-financial information.

Priorities related to non-financial statements include transition plans, explanations of uncertainties surrounding climate-related targets, and reporting on greenhouse gas emissions. The declaration also emphasised the significance of disclosures in accordance with Article 8 of the Taxonomy Regulation.

National enforcers will incorporate the priorities into their examinations of the 2022 annual financial reports of listed companies and ESMA will report on its findings in Spring 2024.

France

AMF analysed listed companies' taxonomy reporting

The Autorité des Marchés Financiers (AMF) published two analyses of listed companies' taxonomy and climate-related reporting in financial statements (9 Nov 2022). Almost all companies in the sample published the required eligibility indicators in their non-financial performance statement. While the majority accompanied these with contextual information, the information was heterogenous, limiting comparability.

The AMF also found that while the entire sample had announced climate commitments, the operational and financial translation of these commitments in the financial statements was not always clear and there was limited communication on the assumptions made.

Key takeaways

- The CSRD will shortly enter into force. EU corporates and non-EU corporates that have activities in the EU should determine if they are in scope of the rules and, if so, the date by which they will need to comply.
- A key challenge for large corporates is navigating the increasingly complex disclosure landscape across jurisdictions. Many corporates will look to comply with the ISSB disclosure framework (once it is finalised). It is expected some jurisdictions (such as the UK) will directly adopt the framework whilst others (such as the EU and US) will develop their own reporting regimes aligned to the framework.
- There is also overlap between TCFD disclosures and other disclosure regimes or proposed regimes. For example, in the UK, it is anticipated that existing TCFD-aligned disclosure rules will be replaced by a requirement for certain companies to disclose in accordance with ISSB standards.
- Given the focus placed by the market and stakeholders on corporates providing accurate and complete sustainability-related disclosures, firms will need to ensure that they have sound governance and data processes in place.

Other papers

- The IFRS Foundation and CDP, the not-for-profit organisation which runs the global environmental disclosure platform for corporations, announced that CDP will incorporate ISSB's climate-related disclosure standard into its global environmental disclosure platform (8 Nov 2022).

Climate risk management

Financial services firms expected to continue to develop their capabilities in climate risk management and scenario analysis

EU

FS-only

ECB deadlines for banks to address climate risks

The European Central Bank (ECB) published the results of its thematic review on climate-related and environmental risks (2 Nov 2022). It concluded that banks lack sufficiently sophisticated methodologies and granular information on climate and environmental risk. 55% of banks have devised practices, but show deficiencies in effective execution of their climate-related action plans and 96% of banks lack the ability to identify the magnitude of climate and environmental risks.

By March 2023, banks will be expected to have adequate categorisation of climate and environmental risks and a full impact assessment on their activities. By end-2023, banks will be expected to implement climate and environmental risks' inclusion in banks' governance, strategy, and risk management. By end-2024, banks will be expected to meet all remaining supervisory expectations, including full integration in the Internal Capital Adequacy Assessment Process (ICAAP) and stress testing.

Int.

FS-only

ISSB confirmed that companies will be required to use climate-related scenario analysis to inform resilience analysis

At a supplementary board meeting (1 Nov 2022), the ISSB agreed that companies will be required to use climate-related scenario analysis to report on climate resilience and to identify climate-related risks and opportunities to support their disclosures. At a minimum, an entity would need to undertake qualitative scenario analysis. The ISSB will build upon TCFD guidance and provide guidance on which climate scenarios an entity should use.

Int.

FS-only

NGFS and FSB report on findings from climate scenario analyses

The Report found that the Network for Greening the Financial System (NGFS) scenarios play a critical role in providing reference climate scenarios and supporting financial authorities' climate scenario exercises (15 Nov 2022).

The Report noted that measures of exposure and vulnerability are likely understated. It raised the concern that many exercises do not capture second-order effects, potential non-linearities in climate-related risks, and potentially large sources of risk. Furthermore, it highlighted that exercises are still considered exploratory and, in most cases, do not translate to policy action.

EU

FS-only

EBA report lays the foundation for ESG risks to be integrated into the SREP of EU investment firms

The European Banking Authority (EBA) published a report on the integration of ESG risks in the supervision of investment firms (24 Oct 2022). This builds on the June 2021 EBA report on the management and supervision of ESG risks for credit institutions and investment firms.

In particular, it provided an initial assessment of how ESG risks could be included in the supervisory review and evaluation process (SREP) of investment firms. The EBA recommended a gradual approach, prioritising the recognition of ESG risks in investment firms' strategies, governance arrangements and internal processes, and later incorporating them in the assessments of risks to capital and liquidity.

Key takeaways

- ECB supervisors – and the UK PRA – have emphasised that "foundational tasks", such as improving banks' climate risk management capabilities, scenario analysis and data are crucial components of the supervisory response to climate change (for the UK, these findings also apply to insurers) . Recent thematic reviews published by the ECB and the PRA demonstrate that firms still have a long way to go on all of those foundational tasks.
- Assessments that have been made of the resilience of banks to climate risk may have been flattered by relatively benign scenarios. Further work by both policy makers and firms is needed in order to better understand, for example, the impact of more severe scenarios and second round effects. Firms should take this into account within their risk assessment work.
- EU investment firms should review the EBA report and consider the extent to which they are exposed to the ESG risks that are discussed. While it is only an initial report, firms can expect increased supervision on their management of ESG risks in future.

Further recent reading from the ECRS

- Blog: Emerging climate-related risks, 21 Nov 2022.
- Blog: Climate and bank capital requirements: where now and where next?, 31 Oct 2022.

Nature and pollution

Increasing attention to nature risk and pollution, including possibly significant changes ahead for automotive industry

Int.

Updated TNFD framework for disclosing nature risks available to pilot

The TNFD launched the third version of its framework (beta v0.3) (4 Nov 2022). This market-led initiative aims to develop a science-based risk management and disclosure framework for organisations.

The new release draws on market feedback on previous beta releases. Over 130 corporates and financial institutions are now testing the framework. The new components in beta v0.3 include (i) updates and additions to concepts and definitions; (ii) enhancements to the Locate, Evaluate, Assess and Prepare (LEAP) approach; (iii) further development of the approach to metrics and targets; and (iv) additional guidance on the disclosure recommendations for financial institutions.

The Beta v0.4 is expected in March 2023, with the final release due in September 2023.

EU

EC proposals on air quality and waste water

The EC published proposals for a Directive on ambient air quality and cleaner air and a Directive on urban wastewater treatment (26 Oct 2022).

The proposals aim to provide return on investment due to their positive effects on health, energy savings, food production, industry, and biodiversity. The EC views the proposals as a significant step towards achieving the European Green Deal's goal of a pollution-free environment by 2050.

EU

EU first "Fit for 55" agreement will end the sale of new CO2 emitting cars in Europe by 2035

The EU Parliament and the Council agreed legislation that all newly manufactured automobiles and vans registered in Europe will be emission-free by 2035 (28 Oct 2022). As a transitional step, the rules will require that new vans and vehicles lower their average emissions by 50% and 55%, respectively, by 2030. The provisional agreement will need to be formally adopted by the EU Parliament and the Council before entering into force.

EU

EC proposed standards to reduce air pollution from new motor vehicles sold in the EU

The EC published a proposal on new Euro 7 standards on emission limits for all motor vehicles (10 Nov 2022). The new rules are fuel- and technology neutral, and the limits will be the same regardless of whether the vehicle uses petrol, diesel, electric drive-trains, or alternative fuels.

The EC proposals included (i) limits for previously unregulated pollutants, such as nitrous oxide emissions from heavy-duty vehicles; (ii) regulation of emissions from brakes and tyres, in addition to exhaust pipe emissions; (iii) regulation of the durability of car and van batteries intended to increase consumer confidence in electric vehicles; and (iv) using sensors inside vehicles to measure emissions to ensure that vehicles are not tampered with.

The proposals will now go to the European Parliament and Council to be negotiated.

Key takeaways

- Although climate risk has dominated recent supervisory and regulatory action and interventions, increasing attention is now being paid to nature risk. This trend will continue with COP15 on biodiversity being held in Montreal starting on 7 December 2022.
- From a reporting perspective, the TNFD framework will become a leading approach for nature-related disclosures. v0.3 of the framework is the most detailed yet and provides a number of dimensions across which firms can start to engage. Nature risk is an important issue in its own right, but is also a crucial component of any strategy to address climate risk – including through net zero transition plans.
- Alongside the development of requirements, the EU is moving forward with initiatives under its Green Deal strategy to address pollution. Car manufacturers selling automobiles and vans registered in the EU will need to comply with significant, new requirements under the first "Fit for 55" agreement and understand how EU proposals to reduce air pollution from new motor vehicles will affect their business.

Further recent reading from the ECRS

- Measure to manage: nature-related risks and opportunities, TNFD framework beta release V0.3, 4 Nov 2022.

Other papers

- The EU signed five Memoranda of Understanding for Forest Partnerships with Guyana, Mongolia, the Republic of Congo, Uganda and Zambia, intended to reverse deforestation and enhance climate and biodiversity protection (8 Nov 2022).

Energy and food

Measures to support energy and food security, and decarbonisation in the EU

EU

EC proposal to accelerate renewables permitting procedures, and to support the transition away from Russian gas

The EC proposed a new temporary emergency regulation to accelerate the deployment of renewable energy sources (9 Nov 2022). It contains proposals in relation to renewable energy plants, solar energy, repowering existing clean energy plants, and heat pumps.

Once in force, the regulation would apply for one year, covering the time needed to adopt and transpose the Renewable Energy Directive, which is currently being negotiated.

EU

Recommendations to ACER on EU energy infrastructure

The European Scientific Advisory Board on Climate Change provided recommendations to the Agency for the Cooperation of Energy Regulators (ACER) on guidelines for scenarios to be used for network development planning (16 Nov 2022).

These are intended to ensure that the planning process for trans-European energy networks supports the necessary energy transition to climate neutrality and resilience in the EU by 2050, particularly as energy supply and use are responsible for 77% of the EU's total greenhouse gas emissions.

EU

EC invests 3 bn EUR in clean tech projects

The EC launched the third call for large-scale projects under the EU Innovation Fund (3 Nov 2022). This is intended to boost the deployment of industrial solutions to decarbonise Europe. With a special focus on the priorities of the REPowerEU Plan, the call is intended to provide additional support towards ending the EU's dependence on Russian fossil fuels.

EU

EC Communication on fertilisers intended to support food security

The EC published a Communication and Annexes on ensuring the availability and affordability of fertilisers (9 Nov 2022). The production and cost of fertilisers largely depend upon natural gas. Russia's invasion of Ukraine has affected food security and food prices. The Communication provides actions intended to help farmers optimise their fertiliser use and reduce their dependences while securing yields. It also includes actions intended to support vulnerable countries and improve global food security.

Key takeaways

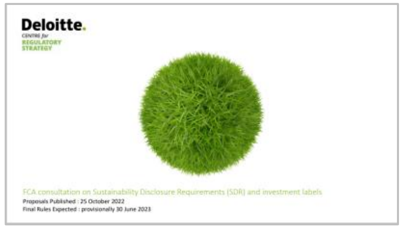
- Russia's invasion of Ukraine has disrupted oil and gas supplies to European countries, raising concern about energy and food resilience and security. Resulting higher energy prices have compounded a cost-of-living crisis, providing an additional driver for Government action.
- EU President Ursula von der Leyen committed the EU to "doubling-down" on renewables to increase energy security. EU measures in relation to energy and food are also intended to support decarbonisation and promote resilience and security.

Other papers

- UN organisations, shipowners and unions launched an action plan to upskill the global seafaring workforce (9 Nov 2022). Research suggests that as many as 800,000 seafarers will require carbon upskilling by the mid-2030s. The Action Plan makes recommendations for industry, Governments, seafarer unions and academia (including training providers).

Further reading

Recent publications on sustainable finance from the Deloitte ECRS



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