February 10, 2017

Comments on the “Recommendations of the Task Force on Climate-related Financial Disclosure”, issued by the Task Force on Climate-related Financial Disclosure (“TCFD”)

Japanese Bankers Association

We, the Japanese Bankers Association (“JBA”), would like to express our gratitude for this opportunity to comment on the “Recommendations of the Task Force on Climate-related Financial Disclosure”, issued on December 14, 2016 by the Task Force on Climate-related Financial Disclosure (“TCFD”).

We respectfully expect that the following comments will contribute to your further discussion.

[General comments]

We support the TCFD’s recommendation to disclose climate-related financial risks on a voluntary basis. While we understand the objectives of quantifying and disclosing financial implications of climate-related risks, the TCFD should give a certain latitude to each entity so as to disclose in line with the actual manners in each jurisdiction, because environment policy, industrial policy, business structure and disclosure rules vary across jurisdictions.

To date, in general, entities lack experience in measuring financial implications of climate-related risks. When we rush to measure and disclose climate-related financial risk, it may result in misleading disclosure against investors as users. It is our concern that, in such cases, specific industries and assets may experience an excessive increase in stranded assets, which could rather undermine the soundness of the financial system. It is therefore necessary to pay sufficient attention so that the climate-related disclosure framework will not be mandatory.

Furthermore, given the current high-level guidance, if entities individually try working on disclosure in accordance with the guidance, differences in their definitions of climate-related risks or compositions of assets could lead incomparable and misleading descriptions. To enhance comparability, more specific guidance or templates, etc. should be provided from TCFD.

In addition, while banks will need appropriate disclosure by their customers in order to measure and disclose climate-related risks, it would be impossible for them to promptly collect sufficient information because most of customers, especially borrowers, are an unlisted company which is not subject to the climate-related disclosure framework. In this view, it should be noted that banks will need a substantial period of time to implement measurement and disclosure of climate-related risks.

[Individual comments]

1. Recommendations and guidance for all sectors

(1) Climate-related opportunities

It cannot be said that disclosure of "climate-related opportunities" is not relevant to the TCFD's objective to ensure the financial system stability. However, the priority of disclosing such climate-related opportunities is lower than that of quantifying climate-related risks and disclosing financial impacts thereof. In this view, the TCFD should give due regard so that the disclosure of climate-related opportunities does not impose excessive burdens.

Furthermore, in order to promote prevalence of measurement and disclosure of climate-related opportunities, TCFD should clarify measurement and disclosure approaches for climate-related opportunities from the perspectives of both the preparer and user side.

(2) Development of climate-related scenarios

Climate-related scenarios should be consistent with the treatment of environment standards and risk management approaches in each entity's jurisdiction and should be simple and practical as much as possible. Banks determine their business strategy in reference to scenario analysis based on their own risk characteristics and expertise judgments. Given this, if scenario analysis is to be performed, discretion should be given to banks with respect to the development of scenarios. If a common and detailed data is required for the scenarios without considering data availability or national legislation of respective banks' jurisdictions, scenario analysis may rather produce inaccurate results. For example, even where a 2℃ scenario is adopted, each jurisdiction sets individual targets and applies different base points in time. Such a unified scenario analysis which does not take into account such backgrounds, if conducted, may result in overestimation or underestimation of climate-related risks, which is not a preferable outcome for financial system stability.

(3) Risk management

Some guidelines on climate-related risk measurement methodologies and models should be provided. Even if scenarios for climate-related risks are set, it would be difficult to ensure comparability of such risks even within the same business sector if quantitative analysis methodologies vary significantly. Given that legislation and policy concerning climate-related risks varies across jurisdictions as mentioned above, it is necessary for the TCFD to provide certain risk measurement guidelines, although application of a one-size-fits-all risk measurement model should be avoided.

(4) Comparability of disclosure

Considering the significantly varied portfolio mix among banking entities, it is not meaningful comparison of climate-related risks by comparing the accumulated each corporate's climate risk nor the aggregated exposures to climate-related asset

Therefore, the objective of the TCFD, ensuring comparable and reliable disclosures would not be achieved. Furthermore, banks have a number of and a variety of customers most of which are unlisted companies, and they are not within the scope of this disclosure. Accordingly, it is difficult in practice to collect and assess climate-related risks information in accordance with detailed standards on an entity-by-entity basis. In light of the purpose of climate-related financial risk disclosures, such disclosures should be limited to industries or assets which are recognized as being highly exposed to climate-related risks on a global basis.

2. Supplemental guidance

The following climate-related risks should be excluded from the scope of measurement and disclosure.

① Investment businesses

Investment business should be exempted from the climate-related risk measurement and disclosure, because it is impractical to measure climate-related risks associated with investment business by banks. In the case of investments as a limited partner ("LP") which is a common activity for banks, for example, it is difficult in practice to assess climate-related risks of bank's investment interests to the fund because only a part of investees from the fund are identified when a LP investment is decided by banks. In addition, it is difficult to evaluate a climate-related risk which materializes at an investee after the execution of LP investment because the bank's financial impact is based on cash flow of dividends from funds which relies on the multiple investees' performances for the accounting purpose. It is therefore impractical to measure and disclose climate-related risks posed to the financial system by investment interests.

② Exposures to emerging countries

In emerging countries, it is not always possible to invest in optimal facilities, etc. in terms of climate-related risks due to the development level of economy and infrastructure. Particularly in low-income nations and island nations, etc., it should be impossible to introduce advanced power generating facilities in the first place. Furthermore, there are many cases in emerging countries where disclosure is insufficient, and it is expected to take a considerable amount of time to, in particular, enhance disclosure of climate-related financial risks. This, as a result, would discourage banks from providing credit to emerging countries and thus may undermine long-term economic growth for these countries.

③ Physical risks

Taking into consideration that companies are hedging most of physical climate-related risks through general insurance, significant climate-related risks are to be already addressed in the financial system through actions taken by companies. To additionally require companies other than general insurers to measure and disclose physical risks would impose multiple and excessive burden on those companies.

The Annex describes that "Banks should consider characterizing their climate-related risks in the context of traditional banking industry risk categories such as credit risk, market risk, liquidity risk, and operational risk" (supplemental guidance; p.21). It is requested that consistency with Basel Committee's framework will be clarified in this respect. For example, it is unclear how to define and assess climate-related risks in the context of the existing risk categories when there is a lack of, or constraint on, availability of data (e.g. loss ratios).

3. Scenario analysis

Disclosure of scenario analysis results should be considered carefully. With respect to scenario analysis of climate-related risks, it is difficult to obtain information necessary for developing appropriate risk management methodologies and analysis, which may lead to misleading disclosures for investors. Furthermore, insufficient scenario analysis may give rise to reputational risk in relation to specific portfolios; and as a result, may accelerate deterioration of banks' investment and financing assets (which reflect the quality of assets held by corporates) and ultimately may cause adverse effects on the financial system.

If it is determined to disclose scenario analysis results, it is preferable that the TCFD add global best practices to be referenced by disclosing entities when conducting scenario analysis to the Annex "Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures".

In case companies themselves are required to forecast and disclose that scenarios' (e.g. 2℃ scenario) impact on their financial statements, from the viewpoint of preparers, it is assumed that they will face uncertainty in forecast and difficulty in developing internal procedures for making disclosure decisions at the initial stage that climate-related risk disclosure practice is not established or sophisticated.

On the other hand, from the viewpoint of users, it is assumed that they will have difficulty in assessing reliability of the content of individual companies' disclosure in cases of simplified disclosure (e.g. a case where it is only described that "there is no significant impact caused by climate change").

4. Carbon-related assets in the financial sector

It is described in the Annex (supplemental guidance; note in p.20) that "The Task Force believes further work is needed on defining carbon-related assets and their potential financial impacts." In doing so, it is necessary to take into consideration, among other things, disclosure standards of each jurisdiction and actual business conditions of banks and at the same time pay attention not to impose an excessive burden on preparers. While the TCFD's recommendations will be treated as voluntary disclosure guidelines for companies, the recommendations may not promote the climate related financial risk disclosures unless they allow disclosures in accordance with the national disclosure standards and banks' actual business conditions (e.g. industry categorization of loan assets is not necessarily based on the Global Industry Classification Standard ("GICS")) because otherwise companies will be subjected to increased disclosure burdens.

In addition, the task owner of "further work" (e.g. TCFD or individual companies) should also be clarified. If the TCFD will act as the task owner, it is recommended to consider publishing additional definitions of carbon-related assets going forward.

From the perspective of comparability, disclosure of exposures to carbon-related assets should be limited to those assets which are designated as having high climate-related risks under the existing disclosure framework or other relevant frameworks. It is our concern that under the TCFD's proposed recommendations, exposures to those carbon-related assets for well-advanced and environmentally-conscious facilities and not sufficient ones will be treated in the same way even within the same industry.

5. Additional feedback

[Major considerations and areas for further work]

Although the Recommendations refers to accounting considerations at describing climate-related risk in the financial filings, but do not give clear guidance on the relationship between accounting rules (e.g. impairment accounting) and climate-related risks. Disclosure of climate-related risks may not be promoted unless such relationship is made clear. Therefore, the TCFD should clarify the relationship between accounting rules (e.g. impairment accounting) and climate-related risks.