

Submission

to the

**Economic Development, Science
and Innovation Committee**

on the

**Financial Sector (Climate-related
Disclosures and Other Matters)
Amendment Bill**

28 May 2021

About NZBA

The New Zealand Bankers' Association (**NZBA**) is the voice of the banking industry. We work with our member banks on non-competitive issues to tell the industry's story and develop and promote policy outcomes that deliver for New Zealanders.

The following seventeen registered banks in New Zealand are members of NZBA:

- ANZ Bank New Zealand Limited
- ASB Bank Limited
- Bank of China (NZ) Limited
- Bank of New Zealand
- China Construction Bank
- Citibank N.A.
- The Co-operative Bank Limited
- Heartland Bank Limited
- The Hongkong and Shanghai Banking Corporation Limited
- Industrial and Commercial Bank of China (New Zealand) Limited
- JPMorgan Chase Bank N.A.
- Kiwibank Limited
- MUFG Bank Ltd
- Rabobank New Zealand Limited
- SBS Bank
- TSB Bank Limited
- Westpac New Zealand Limited

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Executive Summary

NZBA welcomes the opportunity to submit to the Economic Development, Science and Innovation Committee (the **Committee**) on the Financial Sector (Climate-related Disclosures and Other Matters) Amendment Bill (the **Bill**). NZBA commends the work that has gone into developing the Bill.

NZBA supports the policy underpinning the Bill – to introduce mandatory annual disclosures of financially material climate-related risks and opportunities for most financial market participants. The policy reflects the increasing and urgent need to mitigate the significant effects of climate change. As noted in the Bill's explanatory note, financial markets can play a major part in shifting investment towards low-emission, resilient development pathways, assisted by the disclosure to investors of consistent, comparable, reliable, and clear information about climate-related risks and opportunities.

NZBA members will benefit from a strong regulatory regime that produces high-quality disclosures from listed issuers. While NZBA supports the underpinning policy, and is committed to producing high-quality climate risk disclosures, NZBA proposes several amendments to the Bill to ensure that clear, certain and practical requirements are established. This is important not just for our members, but for investors and stakeholders:

1. **Commencement:** NZBA welcomes engagement with government on expectations for the first reporting year following publication of climate standards. Given the likely tight timing between publication of the first climate standard(s) and the first reporting obligations, NZBA seeks a constructive approach from government so that expectations from the XRB and FMA take into account practical challenges for banking sector reporting entities.
2. **Multiple reports:** Banks required to report under multiple categories and banking groups which contain more than one reporting entity need flexibility in publication requirements for climate statements to avoid overlapping or confusing reporting for investors. NZBA members seek flexibility allowing them to combine or separate climate statements between foreign registered banks, NZ branches of foreign registered banks, NZ incorporated registered banks and listed holding or parent companies as appropriate.
3. **Fund by fund reporting:** Registered fund managers should have flexibility when reporting at the fund and scheme level. NZBA seeks flexibility to allow managers to provide such fund by fund level information in fund-specific climate statements and/or alongside scheme level disclosures as appropriate.
4. **Overseas subsidiaries:** NZBA proposes that the Bill clarify whether overseas subsidiaries are intended to be included in reporting requirements, particularly given the specification that overseas incorporated registered banks are only required to report in respect of their New Zealand business.
5. **Penalties:** As has been the case in relation to other recently commenced regulatory regimes, constructive engagement between the FMA and the banking sector will be

vital in the early years of the new regime to ensure successful growth of the climate disclosures regime. During these early years, care is warranted in the enforcement of penalties against willing compliers. NZBA proposes that employees not be subject to penalties or imprisonment at this early stage of such a new regulatory regime.

6. **GHG emissions:** NZBA proposes that penalty provisions applicable to assurance of Scope 3 GHG emissions disclosures (if required) should be delayed to allow capability to develop.
7. **FMA:** Given the importance of the FMA's ongoing role in monitoring and enforcement, NZBA would welcome greater clarification in the Bill as to the scope of the FMA's mandate.
8. **Equivalency:** NZBA proposes that the Bill provide a mechanism (for example delegated legislation) to permit overseas reporting entities that are subject to equivalent requirements offshore to rely on those offshore disclosures for their NZ reporting requirements.
9. **Nominee / custodial / trustee roles:** NZBA proposes that the Bill specify that banks operating in custodial, nominee or trustee roles not be required to report on climate risk arising from non-beneficial asset holdings.

NZBA detailed comments

NZBA and its members are committed to engagement on the Bill and with the XRB as this policy development progresses.

1. NZBA welcomes engagement with government on expectations for the first reporting year following publication of climate standards

NZBA welcomes the introduction of reporting following the publication of the XRB's climate standards (expected in late 2022). However, for those with early balance dates, members could be required to publish their first climate statements soon after the publication of the climate standards, which introduces significant pressure to produce high-quality disclosures.

For example, for banks with September balance dates, if the XRB issues its climate standards before September 2022, those banks would be required to keep records for, and produce climate statements in relation to, the financial year 1 October 2022 – 30 September 2023. This would be a challenging turn-around and will be exacerbated in the first year as banks rely on climate risk disclosures from their underlying borrowers/investors to then produce their own disclosures.

NZBA welcomes a constructive approach from government so that expectations from the XRB and FMA align with the practical challenges that banks will have in the first reporting years.

2. Banks required to report under multiple categories and banking groups which contain more than one reporting entity need flexibility in publication requirements for climate statements to avoid overlapping or confusing reporting for investors

Registered banks and their group entities are likely to be classified as climate reporting entities in multiple ways which may result in an unnecessary compliance burden:

- As a “large” registered bank per ss 461O(1)(b) and 461P(1);
- As an **overseas incorporated registered bank with a “large” New Zealand business** per ss 461O(1)(b), 461P(3) and 461P(4);
- As a “large” manager of a registered scheme per ss 461O(2) and 461Q; and/or
- As a **listed issuer of quoted debt or equity securities** per s 461O(1)(a).

The Bill, as currently drafted, will:

- require some members to produce multiple climate statements within their group, often with very significant overlap; and
- potentially require broad worldwide reporting from registered (including foreign) banks or their holding companies that have opted to list in New Zealand, as opposed to solely reporting in respect of the New Zealand business of a foreign bank’s New Zealand branch.

Flexibility in production of reports: NZBA proposes that the Bill should provide greater flexibility to groups of climate reporting entities to determine how to structure their reporting – including, for example, the options to produce one comprehensive climate statement, or multiple climate statements with cross-referencing between them.

For instance, this could be by:

- Preparing a single climate statement for both a locally incorporated registered bank and the New Zealand branch business of its overseas incorporated registered bank parent or the business of its New Zealand listed holding or parent company, including sufficient information to meet the disclosure requirements for each climate reporting entity but doing so in a consolidated and easily accessible manner.
- For a group with an overseas incorporated registered bank that is New Zealand listed, preparing one or more climate statements for the New Zealand branch business and any locally incorporated registered bank in the group, and a separate climate statement with any additional information required for the listed overseas incorporated registered bank. This may provide more consistency and comparability with the climate statements produced by other registered bank groups.

- Preparing separate climate statements addressing the New Zealand branch of an overseas incorporated registered bank, and the remainder of the New Zealand business of the group. This may be helpful for investors where different aspects of the group's New Zealand business are undertaken using different branding.

Where a group's entities have similar risk profiles and holdings, preparing multiple overlapping reports would often be an unnecessary undertaking and would not adequately reflect those differences. Multiple, overlapping and repetitive climate statements risk being unclear to persons who wish to use them, particularly where other group reporting is ordinarily presented on a consolidated basis (e.g. financial statements). Further, the corporate structures of registered banks and the groups of which they form part vary considerably in the New Zealand market. Closely prescribing what reports need to be prepared by each entity could limit the feasibility of those corporate structures and would create unnecessary compliance costs.

A number of banks that have undertaken voluntary TCFD reporting already publish their results in a standalone document alongside the relevant Reserve Bank disclosure statement, and this approach may be effectively used to report on multiple climate reporting entities. This also aligns with the TCFD's recommendation to publish Climate Statements alongside financial reporting and makes the information accessible for a broader audience.

NZBA proposes the **below amendment** seeking flexibility in reporting. The effect of the suggested amendment is to still require climate reporting disclosure to be produced for every bank registration level and each reporting entity in a group, but to provide that disclosures at different reporting levels and for different reporting entities in the same group may be included in the same document. This allows for flexibility on the number of reports to be produced by each entity and by reporting entities within the same group.

Proposed amendment:

New section: Climate statements and group climate statements may be in the same document

(1) Any climate statements or group climate statements that must be completed by a member of a group required under sections 461W to 461Z in relation to a balance date may be included in a separate document or in the same document as one or more other climate statements or group climate statements required under sections 461W to 461Z for any other climate reporting entity in that group.

Banks that are also registered scheme managers: Registered banks may have subsidiaries that are registered scheme managers and will be climate reporting entities under s 461O(2). NZBA seeks flexibility as to whether banks are required to publish separate climate statements in respect of their banking activities and their investment activities, as appropriate depending on their climate risk profile for these different activities. Accordingly members could prepare a single climate statement with multiple sections, a

single climate statement with cross-referencing between sections, or multiple climate statements (which may also cross-reference each other).

3. Registered fund managers should have flexibility when reporting at the fund and scheme level

The requirement that managers of registered schemes report in relation to each separate fund is significant. NZBA appreciates that the proposed requirement to report at a fund by fund level recognises that each fund will have a different climate risk profile and so disclosures at this level will assist users to elect to allocate capital to funds that are actively managing climate risk. NZBA seeks flexibility to allow managers to provide such fund by fund level information in fund-specific climate statements and/or alongside scheme level disclosures as appropriate.

4. Clarification on overseas subsidiaries required

NZBA considers that references to “subsidiary” in the Bill as presently drafted could include overseas companies. This may cause confusion regarding the scope of reporting in relation to large overseas registered banks (which are only required to report in relation to their (or their group’s) *New Zealand* business) that are also listed issuers (and therefore required to produce group climate statements covering all subsidiaries). If “subsidiary” includes overseas entities, these requirements will be inconsistent.

The lack of clarity results from the new definition of “group” in the FMCA as it applies to the new Part 7A, subpart 3 (s 5(2)(b) of the Bill). The new definition of “group” is “a group comprising a climate reporting entity and its subsidiaries”. The definition of “subsidiaries” is then expressly amended by s 5(3) of the Bill to read “in Parts 7 and 7A, includes any entity that is classified as a subsidiary in any applicable financial reporting standard”. It appears that the intention may be to allow the XRB the discretion to specify the scope of subsidiary reporting in its climate standards, including to require overseas subsidiaries. However technically “financial reporting standard[s]” (per the above mandate) do not extend to climate standards (see s 5(1) Financial Reporting Act).

It would be preferable to have clarity on this scope in the Bill given the clear indications regarding overseas banks reporting only on their New Zealand business. This is also important given that an “entity” under both the FMCA and the Financial Reporting Act may include a company or other body corporate, therefore taking into account overseas companies; and a “company” under the FMCA expressly includes overseas companies (s 6 FMCA).

5. Care warranted in enforcement of penalties in early years against reporting entities who are willing compliers to ensure successful growth of climate disclosures regime

The penalties contained in the Bill are intentionally on a par with the liability regime for breaches of other parts of the Financial Markets Conduct Act and are significant, with non-compliant entities and individuals subject to potential pecuniary penalties and/or imprisonment. Members are concerned that such significant penalties may in the early years of reporting deter entities from reporting the depth of information that will make disclosures useful for end users in favour of generic statements of risk. For example, in the 2019 discussion document on the proposals, officials recognised that “*it is almost inevitable that the quality of reporting will initially be of widely varying quality*” and “*the overall standard of reporting will increase over time*” due to increasing experience and availability of guidance.¹

Our members have considered whether to seek a delay in the application of penalties for the first reporting years. Conscious of the urgency of the need for action on climate change, we do not seek a formal delay to the penalty provisions (aside from as set out at #6 below). Our members want to support the introduction of mandatory climate reporting in New Zealand and consider that banks will play a key enabler role through our engagement on climate reporting with our customers. Our expectation is therefore that:

- the FMA will take a constructive approach in encouraging disclosure in the initial years and work with willing compliers to develop and improve climate reporting under the new regime. During these early years, care is warranted in the enforcement of penalties against willing compliers; and
- the XRB will indicate in its climate standards where a ‘comply or explain’ approach might be taken by reporting entities without exposing those entities to enforcement.

Employee liability: Separately, members ask that the Committee reconsiders whether to retain the proposal for employee liability where there is a failure to comply with a requirement to provide information to an assurance practitioner (s 461ZK). Section 39 of the Financial Reporting Act 2013 imposes liability for failure to provide requirement information to an auditor, but members consider that the extension of penalties to employees in the Bill is unduly onerous where the regime is so new, and could make working in this area unattractive at a time when where organisations are seeking to develop their capability and capacity within challenging timeframes.

6. Penalty provisions applicable to assurance of Scope 3 GHG emissions disclosures (if required) should be delayed to allow capability to develop

NZBA supports the disclosure of GHG emissions as part of the reporting to be required from

¹ <https://environment.govt.nz/assets/Publications/Files/Climate-related-financial-disclosures-discussion-document.pdf>

listed issuers (to be determined by XRB). However, members are cognisant that disclosure of GHG emissions across a lending portfolio requires significant aggregation of GHG emissions data produced by borrowers. Such 'downstream' disclosures by borrowers or investees may include subsidiaries of foreign multinationals, overseas investments and/or private investments beyond the scope of the disclosure requirements.

These challenges are particularly prevalent in respect of Scope 3 emissions, which are significantly more difficult to define and measure than Scope 1 and 2 emissions. Members are not aware of accepted standards of practice for the assurance of GHG emissions across a lending portfolio.

Given the work that still needs to be done to allow banks to properly disclose and assure Scope 3 emissions, NZBA submits that the enforcement of penalties in relation to assurance of Scope 3 emissions should be delayed at least 12 months. If a delay to penalties is not supported, we request that the use of penalties by FMA in the early stages of the regime be considered in light of potential data gaps and the need for entities and assurance professionals to build up the necessary information. This would not delay any requirement to report Scope 3 emissions, but entities would be allowed a period of continuous improvement before facing potential liability.

7. Greater clarity on role of the FMA welcomed

The FMA is mandated to regulate CRD assurance bodies (s 461ZP) and assurance professionals (s 461ZE). The FMA is also intended to have enforcement responsibility for breaches of the legislation.² However, the Bill does not discuss the role of the FMA in its monitoring function, and associated activities related to the monitoring function, such as the publishing of annual monitoring results for the sector. The inclusion of a section discussing the role of the FMA in supporting and overseeing the requirements of the Bill ties in with statements from MBIE that '*The Financial Markets Authority will be responsible for the independent monitoring and enforcement of the relevant reporting entities' compliance with the new reporting standards*'.³ NZBA proposes that the Bill articulate more specifically the role of the FMA in supporting and overseeing the disclosure regime.

8. Future-proofing available through recognition of equivalency for overseas reporting entities

In order to future-proof the legislation, NZBA proposes that the Bill provide a mechanism (e.g. by way of delegated legislation) to permit overseas reporting entities that are subject to equivalent requirements offshore to rely on those offshore disclosures for their NZ reporting requirements. Such disclosures could then reflect any adjustments or additional emphasis for specific New Zealand risk to make sure they were useful to end-users. In this regard,

² <https://environment.govt.nz/assets/Publications/Cabinet-papers-briefings-and-minutes/cabinet-paper-climate-related-financial-disclosures.pdf>

³ <https://www.mbie.govt.nz/about/news/introduction-of-mandatory-climate-related-disclosures/>

NZBA notes Cabinet's reference to a potential class exemption for dual listed issuers with a secondary NZX listing.⁴

9. Clarity required for banks acting in custodial, nominee or trustee roles

NZBA proposes that the Bill specify that banks operating in custodial, nominee or trustee roles not be required to report on climate risk arising from legal, but non-beneficial asset holdings. Assets that are legally held for separate beneficial owners in these situations do not involve any investment discretion by the bank and do not form part of a bank's risk portfolio. Such holdings should be outside the scope of the regime.

⁴ <https://environment.govt.nz/assets/Publications/Cabinet-papers-briefings-and-minutes/cabinet-paper-climate-related-financial-disclosures.pdf> at [56]