Mandatory climate-related disclosure heats up: the CSA seeks comments on national instrument

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The Canadian Securities Administrators (CSA) is seeking feedback on proposed climate-related disclosure requirements set out in National Instrument 51-107 – Reporting of Climate Change-related Risks (the Proposed Instrument). The Proposed Instrument would introduce new disclosure requirements for all reporting issuers in Canada except for investment funds, issuers of asset-backed securities, designated foreign issuers, SEC foreign issuers, certain exchangeable security issuers, and certain credit support issuers. The integral elements of the Proposed Instrument are described below, followed by an overview of the recent history of climate-related disclosure regulation and guidance by the CSA leading up to the Proposed Instrument.

What you need to know

What?

- The Proposed Instrument is largely consistent with the Task Force on Climate-related Financial Disclosures recommendations (TCFD Recommendations).
- In alignment with the four core elements of TCFD Recommendations, issuers would be required to disclose the following:
    - **Governance** – the board of directors' oversight of climate-related risks and opportunities, as well as management's role in assessing and managing the same.
    - **Strategy** – material climate-related risks and opportunities over three horizons: short, medium, and long term. This includes describing how the identified risks and opportunities impact the issuer's business, strategy, and financial planning.
    - **Risk management** – the issuer's process for identifying and assessing climate-related risks; its processes for managing such risks; and how this process fits into its overall risk management framework.
    - **Metrics and targets** – the metrics and targets used by the issuer for assessing climate-related risks and opportunities, to the extent this information is material. Notably, the issuer would also be required to

disclose, or explain its reason for not disclosing, its Scope 1, Scope 2, and Scope 3 greenhouse gas (GHG) emissions.

- The CSA is also considering making Scope 1 GHG emissions mandatory, without the option to explain the absence of such disclosure. Both of these GHG emissions reporting proposals differ from the TCFD Recommendations, which require disclosure of Scope 1 and Scope 2 GHG emissions. The Proposed Instrument is far broader than an issuer's carbon footprint, however, disclosure of GHG emissions is an essential cross-industry, climate-related metric.
- Unlike TCFD Recommendations, the Proposed Instrument does not require a "scenario analysis" that would require an issuer to discuss how resilient its strategies are to climate-related risks and opportunities, taking into consideration a transition to a lower-carbon economy and scenarios with increased physical climate-related risks.

Why?

- The Proposed Instrument is intended to:
  - assist investors in making more informed investment decisions by enhancing climate-related disclosure;
  - facilitate an "equal playing field" for all issuers through comparable and consistent disclosure;
  - harmonize disclosure frameworks to reduce the costs of reporting across multiple frameworks; and
  - improve access to global markets by aligning Canadian disclosure requirements with the expectations of international investors.

Where?

- The Proposed Instrument would require the disclosure to be included in the issuer's management information circular. If an issuer does not send a management information circular, then the disclosure would be required in its annual information form (AIF), or if it does not file an AIF, then in its annual management's discussion and analysis.

When?

- The Proposed Instrument is not expected to come into force prior to December 31, 2022, and would be phased in over a one-year period or in the case of venture issuers, over a three-year period.
- The comment period on the Proposed Instrument ends on January 17, 2022.

Background

Prior to publishing the Proposed Instrument, CSA Staff Notice 51-358 – Reporting of Climate Change-related Risks (the Staff Notice), which was released on August 1, 2019, was the most recent guidance on climate-related disclosure from the CSA. The Staff Notice built on CSA Staff Notice 51-333 – Environmental Reporting Guidance and together, the two notices provided specific guidance for issuers related to environmental matters. Unlike the Proposed Instrument, neither notice created any new legal

requirements for issuers. Nonetheless, it is clear that the CSA has been monitoring climate change-related risks and the disclosure related thereto for several years.

In the spring of 2021, the CSA conducted a review of the public disclosure practices of 48 large Canadian issuers with respect to climate-related information. The CSA had conducted a similar review prior to the release of the Staff Notice. While the CSA noted that issuers had made marked improvement in addressing the qualitative financial impact of disclosed climate-related risks and were increasingly disclosing climate-related information in voluntary reports, the review also revealed certain shortcomings. First, although 92 per cent of issuers disclosed climate-related risks, an average of 41 per cent of the risks were boilerplate, vague, or incomplete, 25 per cent of disclosures did not address the financial impact of the risks, and no issuers quantified the financial impact of the identified risks. Second, on average, issuers referenced nearly three third-party frameworks in their voluntary reports. Whether the first observation will be addressed by the Proposed Instrument remains to be seen, however, the alignment of the Proposed Instrument with TCFD Recommendations would help address the patchwork of reporting frameworks currently being utilized by Canadian issuers.

The alignment of the Proposed Instrument with TCFD Recommendations comes as no surprise given its emergence as the leading global reporting framework for climate-related financial disclosure. Recently, we published an article addressing the shifting landscape of climate change policy in North America, noting that the CSA, along with the United Stated Securities and Exchange Commission (the SEC), federal and provincial governments, and private sector participants in North America have all moved towards making climate-related risk disclosure mandatory and been influenced by TCFD Recommendations in that regard.

For example, earlier this year, the Ontario Securities Commission noted that improving climate change-related disclosure was a key priority for 2021-2022 and highlighted the Ontario Capital Markets Modernization Taskforce's recommendation to mandate climate change-related disclosure that is compliant with TCFD Recommendations. On a similar note, the SEC is expected to release a proposed rule regarding climate-related disclosure as early as the end of this year. The Chair of the SEC has publicly called upon SEC staff to consider the TCFD Recommendations when developing the proposed rule. As the best practices in climate-related disclosure continue to develop and the CSA and SEC develop their policies regarding mandatory climate-related disclosure, securities regulators will likely soon set new minimum standards for public issuers with respect to climate-related disclosure and the Proposed Instrument offers the first insight into what those minimum standards may look like in Canada.

Understanding GHG emissions

A detailed overview of GHG emissions reporting is beyond the scope of this article, but given the proposed mandatory requirements in the Proposed Instrument, readers should understand the broad strokes of such reporting. The globally accepted standards for reporting GHG emissions are those developed by the Greenhouse Gas Protocol (the Protocol). The Protocol has developed a total of seven standards, however, two have become key: the Corporate Accounting and Reporting Standard (the Corporate Standard) and the Corporate Value Chain (Scope 3) Standard (the Scope 3 Standard), which is a supplement to the Corporate Standard. Together, these two standards create three categories for reporting purposes:

- Scope 1: Direct emissions from owned or controlled sources.
- Scope 2: Indirect emissions from the generation of purchased energy.
- Scope 3: All indirect emissions (not included in Scope 2) that occur in the value chain of the reporting firm, including both upstream and downstream emissions. Viewed another way, the Scope 3 emissions for one firm are the Scope 1 and 2 emissions of another firm. Examples of Scope 3 emissions include production of purchased products (downstream) and the use of the sold products (upstream).

Scope 3 emissions usually represent the majority of an issuer's total GHG emissions. Currently, the TCFD Recommendations include the disclosure of Scope 1, Scope 2, and state that Scope 3 emissions are encouraged but are subject to a materiality assessment.

Takeaways

While the CSA has clearly demonstrated a willingness to mandate climate-related disclosure, the Proposed Instrument remains in its infancy and the ultimate impact on issuers will be determined over the coming years. Nevertheless, at the very least, the Proposed Instrument reflects the international convergence around the TCFD Recommendations and presents a clear trajectory for aligning Canadian securities legislation with such recommendations and creating new mandatory disclosure requirements for issuers.

Members of BLG's Environmental, Environmental, Social & Governance and Climate Change teams have partnered with climate and engineering consultancies to provide clients with expert advice in the area of climate change. As regulators move toward increased climate transparency, our Environmental, ESG and Climate Change experts can ensure issuers remain protected while complying with regulations and meeting the expectations of investors. Reach out to any of the lawyers listed below should you have any questions or concerns regarding the CSA's proposed climate-risk disclosure requirements.

Special thanks to BLG articling student Rachel Summers for her contribution to this article.

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