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***CSA Propose Standardized and More Comprehensive Climate-Related Disclosure***

By Bruno Caron\*\*

On October 18, 2021, as a preamble to COP26, the United Nations Conference on Climate Change in Glasgow, the Canadian Securities Administrators (CSA) published for consultation draft National Instrument 51-107 Disclosure of *Disclosure of Climate-related Matters*<sup>1</sup> (NI 51-107). The CSA also provided explanatory notes in the form of Companion Policy 51-107CP *Disclosure of Climate-related Matters*<sup>2</sup> (CP) and completed this duo with two forms — Form 51-107A Climate-Related Governance Disclosure and Form 51-107B *Climate-Related Strategy, Risk Management and Metrics and Targets Disclosure*. The public has until January 17, 2022, to provide comments on both NI 51-107 and the CP generally and specifically (through a set of 18 questions contained in the Notice of Consultation<sup>3</sup>).

***Background***

Increasingly globally, the effects of climate change are being felt through extreme weather events. These changes in climate create material and transition risks that have financial consequences for businesses and organizations. Insufficient disclosure of these risks and their consequences can lead to unwise investment decisions, asset write-downs and the continuation of environmentally inefficient business practices. As a result, regulators around the world are under increasing pressure to impose a framework on companies to disclose their strategy and mitigation practice with respect to climate risks, but also with regards to related business opportunities.

In Canada, as early as 2010, with CSA Staff Notice 51-333 *Environmental Reporting*

*Guidance*,<sup>4</sup> the CSA provided issuers with environmental disclosure guidance. More recently, in 2019, the CSA published CSA Staff Notice 51-358 *Reporting of Climate Change-related Risks*,<sup>5</sup> in which it reiterated the importance of climate-related disclosure by providing additional guidance in this regard. These directives complemented the general disclosure obligations already contained in National Instrument 51-102 *Continuous Disclosure Obligations*, National Instrument 52-109 *Certification of Disclosure in Issuers' Annual and Interim Filings*, National Instrument 52-110 *Audit Committees* and National Policy 58-201 *Corporate Governance Guidelines*.

In the spring of 2021, the CSA conducted a focused review of climate change-related disclosure produced by reporting issuers and analysed international regulatory developments happening on this front. As part of this review, the CSA noted that climate change-related information presented by issuers was often not complete, consistent, and comparable and that quantitative information was often limited and not necessarily consistent. Staff of the CSA also noted that issuers generally choose their information selectively and according to voluntary standards or frameworks. The CSA have also discovered that the sustainability reporting was often occurring in a vacuum and not necessarily integrated into the issuer's periodic reporting. These findings prompted the publication of NI 51-107 and the CP.

### ***Disclosure Aligned with the Four Core Elements of TCFD Recommendations***

With certain modifications described in the CP, NI 51-107 proposes new climate-related disclosure aligned with the four core elements set-out by the Task Force on Climate-related Financial Disclosures (TCFD) in its June 2017 Recommendations<sup>6</sup> (**TCFD Recommendations**) which includes: (i) governance; (ii) strategy; (iii) risk management; and (iv) metrics and targets.

Over 1,500 organizations, including over 1,340 companies with market capitalization of \$12.6 trillion now use the TCFD Recommendations as a framework for their climate-related disclosure. Currently, regulators in New Zealand, the EU, and the UK are moving toward requiring TCFD disclosure through legislation and regulation. The TCFD was established in 2015 by the Financial Stability Board, an international body that monitors and makes recommendations about the global financial system, to develop a set of voluntary climate-related financial risk disclosures.

### ***Detailed Analysis of NI 51-107***

#### *What to Disclose?*

Part 2 of NI 51-107, Form 51-107A and Form 51-107B organize the disclosure along the four core elements described in the TCFD Recommendations and provide issuers

guidance on when such disclosure is mandatory or optional. New Form 51-107B will also require disclosure of greenhouse gas (GHG) emissions on a comply or explain basis. The table below summarizes the information required by NI 51-107 along the lines of the four core elements. The last column deals with GHG emissions disclosure:

<b>Form 51-107A</b>	<b>Form 51-107B</b>			
<b>Governance</b> (mandatory)	<b>Strategy</b> (only if material)	<b>Risk Management</b> (only if material)	<b>Metrics and Targets (M&amp;T)</b> (only if material)	<b>GHG Emissions</b> (comply or explain)
Describe board’s oversight of climate-related risks and opportunities and management’s role in assessing and managing climate-related risks and opportunities.	Describe climate-related risks and opportunities the organization has identified over the short, medium, and long-term and their impact on businesses, strategy, and financial planning.	Describe the organization’s processes for identifying, assessing and managing climate-related risks and how such processes are integrated into the overall risk management.	<ul style="list-style-type: none"> <li>• Disclose the metrics used to assess climate-related risks and opportunities in line with the issuer’s strategy and risk management process.</li> <li>• Disclose the targets used to manage climate-related risks and opportunities and the issuer’s performance against these targets.</li> </ul>	Disclose issuer’s Scope 1, 2 and 3 GHG emissions and the related risks or the issuer’s reasons for not disclosing this information.

*How to Disclose?*

The specific requirements concerning the nature and form of disclosure are provided in Form 51-107A with respect to governance and in Form 51-107B with respect to strategy, risk management, M&T, and GHG emissions. This disclosure should be

provided in the following public disclosure documents:

- **Governance (Form 51-107A):** In the proxy circular or, if the reporting issuer does not send a proxy circular, its Annual Information Form (AIF) or, if it does not file an AIF, its annual Management's Discussion & Analysis (MD&A). The governance related information is always mandatory.
- **Strategy, Risk Management, M&T and GHG Emissions (Form 51-107B):** In the reporting issuer's AIF, or if it does not file an AIF, in its annual MD&A. The disclosure of information related to strategy, risk management, and M&T is required if material.

Under item 4(a) of Form 51-107B an issuer would be required to disclose each of its Scope 1, Scope 2 and Scope 3 GHG emissions or explain why it did not do so on a "comply or explain" basis. For example, if an issuer discloses its Scope 1 and Scope 2 GHG emissions, but not its Scope 3 GHG emissions, the issuer would be required to explain why it omitted this information. The draft CP indicates that where an issuer elects to omit disclosure of its GHG emissions, it may provide its explanations for such omission in respect of its GHG emissions as a whole, as opposed to a separate explanation for each scope.

For a more in-depth discussion on the carbon footprint calculations and scope of GHG emissions, please see the section below titled "***Suggested Calculation Standard for the Carbon Footprint and Proposed Alternative GHG Emission Disclosure Regime***".

#### *Who Will Disclose?*

Except for certain reporting issuers listed below, all reporting issuers, including venture issuers, will be subject to the reporting requirements of NI 51-107.

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| <p>Issuers <b>Excluded</b> from Application of NI 51-107</p> | <ul style="list-style-type: none"><li>• investment funds</li><li>• issuers of an asset-backed security</li><li>• designated foreign issuers or SEC foreign issuers</li><li>• certain exchangeable security issuers used in cross-border M&amp;A transactions</li><li>• certain credit support issuers and subsidiary entities whose parent company is either: (i) subject to NI 51-107 or (ii) owns securities listed or quoted on a U.S. marketplace and in compliance with U.S. marketplace corporate governance disclosure</li></ul> |
|--|---|

*When to Disclose?*

After the instrument’s adoption, the disclosure requirements will be phased in over a one-year period for non-venture issuers (mainly TSX listed issuers) and over a three-year period for venture issuers (mainly issuers listed on the TSX Venture Exchange and the Canadian Stock Exchange). The CSA anticipates that NI 51-107 will not come into force prior to December 31, 2022.

Assuming NI 51-107 becomes effective on December 31, 2022, and the issuer has a calendar year-end, the following timeline would apply:

<b>Issuer Type</b>	<b>Financial Year Covered</b>	<b>Deadline for Disclosure</b>
Non-venture	FY ending December 31, 2023	March 2024
Venture	FY ending December 31, 2025	April 2026

If a venture issuer graduates to be a non-venture issuer during the period when the instrument targets only non-venture issuers, the disclosure required by NI 51-107 will not apply for the financial years in which it was still a venture issuer.

***Suggested Calculation Standard for the Carbon Footprint and Proposed Alternative GHG Emission Disclosure Regime***

The CSA suggests the use of the GHG Protocol Corporate Standard<sup>7</sup> (**GHG Protocol**), an internationally recognized framework for measuring GHG emissions developed by the World Resources Institute and the World Business Council for Sustainable Development, to measure GHG emissions. If an issuer chooses to use a standard other than the GHG Protocol, it will need to explain in its AIF or, in the absence of one, in its annual MD&A how the standard used compares to the GHG Protocol.

An issuer will be able to incorporate its GHG emission data by reference to another document as long as it clearly identifies the reference document or excerpt of it and such information is filed on SEDAR prior to or simultaneously with the new NI 51-107 disclosure.

The GHG Protocol classifies a company’s emission into three scopes:

- **Scope 1:** These are direct emissions from owned or controlled sources, such as the company’s facilities and the company’s vehicles.
- **Scope 2:** These are indirect emissions from the generation of purchases of energy by the issuer, such as electricity, steam, heating and cooling.

- **Scope 3:** These are all indirect emissions (not included in Scope 2) that occur in the value chain of the reporting company and includes both upstream and downstream emissions.

### *Particularity of Scope 3 Emissions*

Scope 3 emissions are generally difficult to quantify, but often represent the most significant GHG emissions of an issuer. These emissions are divided into 15 categories.

Examples of upstream Scope 3 emissions categories are: purchased goods and services, capital goods, upstream transportation and distribution, waste from operations, business travel, employee commuting and upstream leased assets. Examples of Scope 3 downstream emissions categories are: downstream transportation and distribution, processing of sold products, use of sold products, end-of-life treatment of sold products, downstream leased assets, franchises, and investments.

### *Alternative GHG Emission Disclosure Approach Proposed for Comments*

With respect to the disclosure of GHG emissions, the CSA is consulting on an alternative approach that would only require issuers to make a Scope 1 GHG emissions disclosure (i.e., direct GHG emissions) either a) when that information is material, or b) in all cases. Scope 2 and Scope 3 disclosures would not be mandatory under the alternative approach, but the issuer would have to comply or explain.

### *No Scenario Analysis*

Under the proposed NI 51-107, issuers would not be required to perform scenario analysis aligned with the objectives of the Paris Agreement, such as the International Energy Agency's Net Zero by 2050 Scenario,<sup>8</sup> to assess their GHG emission reduction strategy. The CSA noted that the investment community expressed some concerns about the consistency and comparability of scenario analysis when used without a standardized set of assumptions. The CSA also noted that the costs associated with developing scenario analysis were a concern for issuers. In this respect, the CSA chose to deviate from the TCFD Recommendations, which favor the use of scenario analysis.

### *The Road Ahead*

The stated aim of proposed NI 51-107 is to standardize issuers' climate-related disclosures to allow for a better comparability of the climate-related risks and opportunities facing Canadian issuers. This will allow investors to better price the

financial risks and the opportunities associated with climate change and the race to a net zero carbon economy. In that sense, NI 51-107 provides one piece of the puzzle. The other piece of the puzzle will come when stricter rules will be introduced concerning the financial reporting of issuers. A recent study published in September 2021 by Carbon Tracker and the Climate Accounting Project reviewed the financial statements of 107 companies and found that over 70% of these companies did not indicate whether they had considered climate matters when preparing their 2020 financial statements. This was despite the fact that significant institutional investors had identified these companies as high carbon exposed. The same study also found that 80% of auditors provided no indication of whether or how they had considered material climate matters, such as the impact of emissions reduction targets, changes to regulations, or declining demand for company products in their audits. The focus on climate disclosure provided by NI 51-107 should also be accompanied by new rules targeting improved climate governance with respect to financial reporting and internal controls to guarantee that climate matters are an integral part of any audit plan. Auditors should also be required to provide evidence of the work they did to address climate-related issues, including how they have scrutinized and challenged management climate assumptions and inputs.

While the process leading to the adoption of NI 51-107 continues, the legislative momentum around the world regarding climate-related disclosure keeps growing. This may prompt certain issuers to act now. Effective climate-related disclosures can not only minimize legal risks such as litigation related to insufficient climate-related risk disclosures, but it can also provide competitive advantages such as a lower cost of capital, constructive engagement with shareholders and suppliers, heightened mobilization of employees and stronger relationships with external stakeholders.

## Footnotes

\* **Steven London** has practiced securities and corporate law for over 20 years, currently as the principal of LONDON Business and Securities Law. Steven provides regulatory and legal advice to public and private investment funds and securities industry registrants, in addition to carrying on an M&A practise focused on small and mid-sized businesses. Steven has also served as a Chief Compliance Officer for 10 years. In addition to his law degree, Steven holds an MBA from Ivey Business School at Western University.

\*\* **Bruno Caron** is a well-respected lawyer with a practice primarily focused on corporate law and securities, with particular emphasis on public and private financing, mergers and acquisitions as well as corporate governance. In 2021, *Best Lawyers in Canada* recognized Bruno as a leading lawyer in Securities and Mergers and Acquisitions Law.

Bruno has a particular interest in green financing as a means to mitigate and adapt to the climate change and for the disclosure rules applicable to the risks associated with climate change. He has acted for Sovereign in connection with green bond issuances. Bruno was also nominated by the *Canada Climate Law Initiative* to join the list of Canadian Climate Governance experts.

<sup>1</sup> [https://www.osc.ca/sites/default/files/2021-10/csa\\_20211018\\_51-107\\_disclosure-update.pdf](https://www.osc.ca/sites/default/files/2021-10/csa_20211018_51-107_disclosure-update.pdf)

- 2 <https://lautorite.qc.ca/fileadmin/lautorite/reglementation/valeurs-mobilieres/51-107/2021-10-18/2021oct18-51-107-ig-cons-en.pdf>
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- 7 <https://ghgprotocol.org/sites/default/files/standards/ghg-protocol-revised.pdf>
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