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Investor groups call on companies to reflect climate-related risks in financial reporting

Investors are concerned that companies risk overstating financial statements by failing to include the effects of climate change on profits and assets

LONDON - Today, major investor groups from around the world representing assets worth over \$103 trillion released an [Open Letter on Accounting Standards](#) calling on companies and auditors to fully reflect the effects of climate change in their declared results. In particular they call for compliance with groundbreaking [new guidance](#) from the International Accounting Standards Board (IASB) on the pressing need to reflect climate-related risks in financial reports. The letter was signed by the Principles for Responsible Investment (PRI), the UN Environment Program Finance Initiative (UNEP FI), the UN-convened Net-Zero Asset Owner Alliance initiative, the Institutional Investors Group on Climate Change (IIGCC), Investor Group on Climate Change (IGCC), the Asia Investor Group on Climate Change (AIGCC) and the Pensions and Lifetime Savings Association (PLSA).

Mark Carney, COP 26 Finance Adviser and UN Special Envoy, commented: *“Markets require information to operate effectively – what gets measured gets managed. Investors need to understand how extreme weather events and climate policies to achieve net zero affect business models and what could be the associated financial impact. This requires an improvement in the quantity, quality and comparability of reporting, which, as the IASB has made clear, should be included in the core financial reports issued by companies. As it is increasingly clear that climate change will prompt reassessments of the values of virtually every financial asset, investors have a right to know which companies will be the leaders and the laggards in the climate transition.”*

Today, company accounts typically apply business as usual assumptions - for example they place high values on the future price of fossil fuels and declare a profit on that basis. Yet our planet cannot sustain business as usual.

In the letter, the groups state that companies need to consider material climate change effects in calculating their profits and assets, and in drawing up their accounts more broadly. Investors also insist that the assumptions that companies apply regarding climate change should be consistent with a sustainable world – in other words in line with the goals of the Paris Agreement.

The effects of this change are potentially huge. BP, for example, recently declared a US\$16.8 billion loss, as it recognised that the values it had placed on its assets were inconsistent with climate and other considerations. It also began a review of its future capital expenditure. By following the investor groups demands and taking climate-related risks into consideration in making investments, companies should not be able to exaggerate their true value, and risk generating a pool of ‘stranded assets’, which cannot be exploited without irreparable climate damage.

“The world cannot afford business as usual, but that is what too many companies are currently pricing in with regards to climate change risks,” said PRI CEO Fiona Reynolds. “In order for us to invest properly for the long-term, a sustainable future needs to be factored in when calculating any company’s profits and assets. That is what the IASB statement demands - and so do investors.”

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The letter calls for the following:

- That companies apply the IASB opinion in the letter and the spirit, including showing the key assumptions that have been made with regard to climate-related risks
- That auditors only sign off on financial statements that are consistent with the IASB opinion in the letter and the spirit
- That regulators and civil society work with PRI in enforcing and encouraging these actions
- That henceforward the assumptions made by companies in preparing financial statements under International Financial Reporting Standards be compatible with the Paris Agreement

The investors note that realistic climate assumptions would have major impacts on companies that have understated the effect of climate-related risks. Among the industries most impacted will be those operating in oil and gas, utilities and transportation. In many of these sectors, analysis predicts that other companies will face potential write offs of similar magnitude to those at BP.

Günther Thallinger, Member of the Board of Management Allianz SE and Chair of the Steering Group of the UN-Convened Net-Zero Asset Owner Alliance, commented: *“Climate risks is one of the largest financial risks and therefore material. This is why climate risks affecting financial values and revenues must be taken into account in the financial disclosure of a company. The financial disclosure is the most powerful instrument when it comes to the quality, completeness and consistency of information.”*

Anne Simpson, Interim Managing Investment Director, Board Governance & Sustainability, CalPERS, said: *“Accounting rules were invented so that investors can deploy capital understanding the drivers of risk and return. If the accounts do not capture material climate change risk, then we have smoke and mirrors. We need accounting standards that ensure that companies reporting profits reflect the full costs of those profits. For a long-term investor like CalPERS this is critical as those costs can lead to risk of loss and even bankruptcies. The concept of the accounts being true and fair means climate risk cannot be cloaked in green wash. Company accounts should not allow companies to present a green Ponzi scheme for investors. The IASB guidance is vital to ensure stranded assets are not clutched as a life raft by the desperate. This needs to be picked up by US regulators too so that we have global standards to reflect a global risk.”*

Stephanie Pfeifer, CEO, Institutional Investors Group on Climate Change, explains: *“We face a climate emergency. It’s vitally important that climate change is accurately factored into financial reporting from companies. Guidance from the IASB makes this crystal clear and auditors must ensure they are providing financial markets with information that takes account of climate risk.”*

Emma Herd, Chief Executive Officer of the Investor Group on Climate Change, (Australia/New Zealand) said: *“Australian and New Zealand investors are already using climate disclosure in their core strategies from engagement to ESG integration, but to date the coverage and quality of disclosure has mostly fallen short of investor needs. Companies need to utilise the best guidance and tools to produce the most robust climate disclosure that is consistent with the Paris Agreement goals or risk being discounted in portfolio decisions.”*

Rebecca Wright-Mikula, Executive Director of the Asia Investor Group of Climate Change, said: *“There has already been significant progress and uptake of climate risk disclosure in many Asian markets, but investors are wanting companies to take the next step and better demonstrate how their understanding of climate change exposure is informing their business strategies and governance. The recent publication on climate risk*

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from International Accounting Standards Board, coupled with the emerging guidance and scenarios from local regulators and central banks, are key pathways for companies to improve their disclosure for investors."

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About PRI:

PRI works with its international network of signatories to put the [six Principles for Responsible Investment](#) into practice. Its goals are to understand the investment implications of ESG issues and to support signatories in integrating these issues into investment and ownership decisions. The six Principles were developed by investors and are supported by the United Nations. The PRI does not operate for its own profit; it engages with global policymakers but is not associated with any government; it is supported by, but not part of, the United Nations.

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