

INDIA'S FIRST MAGAZINE ON LEGAL AND CORPORATE AFFAIRS

L E X

WITNESS

Volume 14 Issue 7 | June - July 2024

₹ 100 US \$10 UK £6

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Critical Analysis of the Draft Guidelines regarding Disclosure Framework on Climate related Financial Risks, 2024

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I. INTRODUCTION:

The Reserve Bank of India (RBI), on the 28th February, 2024, released a Draft regulation titled “Draft Disclosure Framework on Climate-related Financial Risks, 2024”¹. The Draft is consequential to the Discussion Paper on Climate Risk and Sustainable Finance² that RBI issued on the 27th July, 2022. Both the Discussion Paper and the Draft Disclosure Framework are built around the Task Force on Climate-related Financial Disclosures (TCFD)³ recommendations.

The Discussion Paper on Climate Risk and Sustainable Finance⁴, highlights Climate Change as a major concern for the Regulated Entities (REs). It outlined the sources and potential impacts of Climate Risks on REs, stressing on the need for appropriate Governance, Strategy, and Risk Management Framework to address these challenges. Effective Climate-related Disclosures by REs are crucial for Stakeholders such as Customers, Investors, and Regulators to comprehend the risks involved and the strategies employed to address such issues. The Disclosures by the REs shall cover the following Four Thematic areas (Pillars) - Governance, Strategy, Risk Management and Metrics and Targets.

The Disclosure Framework applies to:

- a. All Scheduled Commercial Banks (excluding Local Area Banks, Payments Banks and Regional Rural Banks)
- b. All Tier-IV Primary (Urban) Co-operative Banks (UCBs)
- c. All All-India Financial Institutions (viz. EXIM Bank, NABARD, NaBFID, NHB and SIDBI)
- d. All Top and Upper Layer Non-Banking Financial Companies (NBFCs)
- e. Foreign banks for their operation within India
- f. Voluntary for Regulated Entities not covered by (a) to (d).

Encouraging transparency and accountability through the guidelines proposed in the Draft would enable Financial Institutions to proactively manage Climate-related Risks. Moreover, following the Global standards boosts the credibility and reputation of Regulated Entities in the Global market. The purpose of providing a Critical Analysis to this Draft is to contribute to constructive feedback and insights that could improve its quality and enforcement.

Here are some critical observations that could be included in the Draft:



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Thematic Pillar	Issues	Additional Inputs with Solution
Governance	<p>REs need to describe the Board’s oversight of Climate-Related Risks and Opportunities.</p> <p>The Baseline Disclosure of the Governance Thematic Pillar enables REs to establish Management-level Positions or Committees focused on Sustainable Finance and Climate-Related Financial Risks. However, regulatory mandates may not fully prioritize Sustainable Finance over short-term financial gains despite oversight requirements.</p> <p>REs could be provided with more guidance on the Scenario Analysis.</p>	<p>Disclosure should indicate how governance bodies or individuals tasked with managing Climate-Related Risks and Opportunities are represented in their terms of reference, mandates, and role descriptions.</p> <p>To address this concern, REs should introduce incentives such as performance-based bonuses tied to Sustainability targets and Employee Recognition programs. Including Sustainability Metrics in Performance Evaluations is essential. Establishing a Grievance Redressal Committee (GRC) is critical for transparency, regulatory clarity, and market integrity in addressing Sustainability, Climate-related risks, and Ethical conduct grievances.</p> <p>REs should provide frameworks for effective scenario analysis, incorporating best practices such as UNFCCC guidelines for GHG emissions. Guidance on Financial Impact Assessment, Sensitivity Analysis, and Risk Management Strategies is crucial for Entities to address Climate-related risks comprehensively.</p>
Strategy	<p>REs need to describe the Climate-related Risks and Opportunities identified over the Short, Medium and Long term.</p> <p>REs need to describe the Impact of the Climate-related Risks and Opportunities on the Organization’s Businesses, Strategy and Financial Planning.</p> <p>The Enhanced Disclosures under the Pillar of Strategy mandate burdens the REs to disclose current and anticipated mitigation efforts, with need to balance Climate Change mitigation with profitability for market sustenance.</p> <p>Identification/Monitoring of gravity of risks of Climate-related change</p> <p>Need for Carbonization Abatement Plan as a Strategy</p> <p>Complexity in Tasks like Climate-related Risks and Opportunities.</p> <p>The European Union’s Sustainable Finance Disclosure Regulation aims to enable informed Investor decisions and enhance Investor confidence in Sustainable Finance. However, our current disclosure lacks this implementation.</p>	<p>Disclosures could include Industry-based disclosures to identify Climate-related Risks and Opportunities.</p> <p>REs should disclose response strategies to climate-related risks and opportunities, including Transition plans and Methodologies for Climate targets. Financial effects should be disclosed using all reasonable and supportable information available at the reporting date.</p> <p>Regulators could incentivize Innovation in Climate-related reporting by rewarding REs for excellence, encouraging best practices etc.</p> <p>Approach of color coding can be taken to identify climate risks – an illustration is provided below:</p> <p>Purple for very high risks with severe, irreversible Climate impacts; Red for severe, widespread impacts; Yellow for detectable, medium-confidence impacts; and White for non-detectable climate impacts.</p>



	<p>United Kingdom’s Transition Finance and Market Review aims to boost transition finance and analyse Market Dynamics first-hand. This proactive approach is currently absent from our disclosure.</p>	<p>A Carbonization Abatement Plan by REs would involve strategies to reduce Carbon Emissions and mitigate Climate impacts in Operations, Investments, and Lending. This includes financing Low-carbon technologies, enhancing energy efficiency, and incorporating Environmental and Social risk assessments into lending decisions to support a low-carbon economy transition.</p> <p>Regulatory bodies can support entities in managing Climate-related risks by providing comprehensive Technical guidance, Training, and Collaboration opportunities. Industry forums and peer-to-peer networks can facilitate knowledge-sharing and collective improvement in addressing the issues.</p> <p>Prioritizing Investor confidence fosters trust, attracts responsible Investors, and enhances Market integrity for economic stability and growth. Incorporating “stimulating investor confidence” under the Governance Pillar, could significantly enhance REs’ compliance and adherence towards the framework.</p> <p>Including First-hand Market analysis in India’s disclosures is crucial for Stakeholders to understand challenges and opportunities in Transition Finance. Such reviews benchmark Policy Effectiveness, Track Progress, and Identify areas for improvement. Insights into Market dynamics, Investment trends, and Potential barriers are essential for shaping effective strategies and achieving desired outcomes.</p>
<p>Risk Management</p>	<p>Enhanced Disclosures mandate annual disclosure of changes in Climate-related Risk Management processes without a Comparative Analysis.</p> <p>The Monetary Authority of Singapore’s “Environmental Risk Management Guidelines for Banks, Insurers, and Asset Managers” highlighted the need for Financial Institutions to address Environmental risks beyond Climate-related issues, including Reputational risks. Current disclosure framework focuses mainly on Climate risks, potentially overlooking Pollution, Biodiversity Loss, Water Scarcity, and Deforestation. Inconsistent and incomplete disclosures due to limited regulatory coverage of Non-climate environmental risks can damage Stakeholder Trust and Reputation.</p>	<p>Comparative analysis evaluates Current Risk Management against the Previous years’ with alternative strategies, enhancing REs’ adaptation to Climate-related financial risks. It provides insights into its effectiveness and identifies the most suitable strategies for mitigation.</p> <p>Adopting an Integrated approach to Risk Management that considers both Climate and Non-Climatic Environmental risks holistically could be a possible solution.</p>

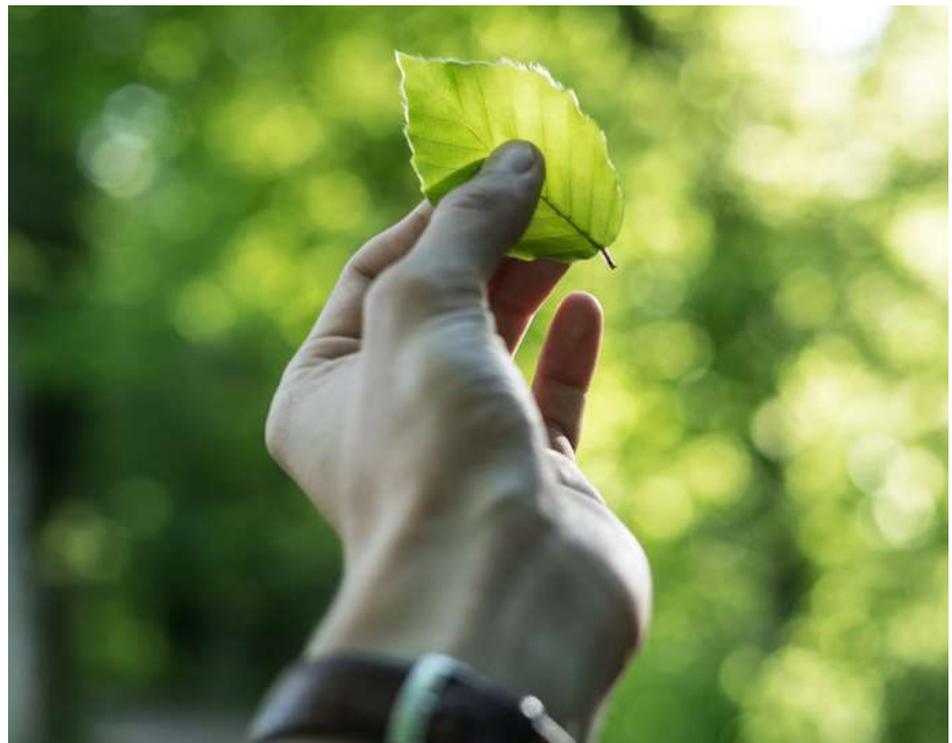
<p>Metrics and Targets</p>	<p>REs must disclose the Metrics used to assess Climate-related risks and Opportunities aligned with their Strategy and Risk Management processes.</p> <p>REs need to disclose the Targets used by the organization to manage Climate-related Risks and Opportunities and Performance against such targets.</p> <p>Enhanced disclosures require REs to justify their inability to calculate and disclose Absolute Gross Financed Emissions, but do not offer alternative approaches for the same.</p>	<p>The Disclosure of Industry-based metrics relevant to a RE's operation model and activities may be included.</p> <p>Disclosure should provide in detail GHG emissions Targets, including Plans for using Carbon Credits to achieve Net Emissions Goals. Requirements should outline the approach to setting and reviewing targets, monitoring progress, and whether sectoral decarbonisation methods were used in Target derivation.</p> <p>To address this, the Framework could provide alternatives such as simplified methodologies using indicators and sector-specific factors, or standardized reporting templates to streamline disclosure. Collaboration among REs within sectors could facilitate knowledge sharing and improve disclosure practices collectively.</p>
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II. STRATEGIC APPROACHES TO ENHANCE CLIMATE AND SUSTAINABILITY COMPLIANCE:

1. Entities face challenges in meeting disclosure requirements due to data limitations, lack of standardized methodologies, and resource constraints. Addressing these challenges would involve improving data reliability through better collection methods, establishing standardized reporting approaches, and allocating adequate resources for compliance.

2. Overlapping disclosures between the Disclosure Framework and Financial reporting can be managed by realigning existing disclosures and cross-referencing relevant information to avoid redundancy.

3. Regulators can incentivize



innovation in Climate-related reporting to integrate risks into overall risk management frameworks, ensuring systematic identification and management alongside financial risks.

4. Further disclosures should specify in detail - the Stakeholder engagement on Climate issues, including strategies, responses to inquiries, and feedback processes.

5. The “Do No Significant Harm” (DNSH) criteria may be included as a strategy which refers to a principle or standard aimed at ensuring that actions, policies, or projects intended to mitigate or adapt to Climate Change do not cause significant negative impacts on People, Ecosystems or the Environment. Implementing the Double Materiality Assessments and DNSH criteria would enhance credibility and ensure Climate actions benefit both Environmental and Social dimensions, promoting Sustainable Finance practices aligned with Global Climate Goals.

6. REs play a crucial role in addressing Climate Change through strategic Loan allocation and Investment decisions. Prioritizing financing for Renewable Energy sources reduces reliance on Fossil Fuels and supports Decarbonisation. Support for energy efficiency initiatives across sectors reduces emissions and enhances sustainability. Investment in Green infrastructure, like Public

transportation and Ecosystem restoration, would further help the environment.

7. REs could facilitate Green finance initiatives, such as Green bonds and Sustainable loans, to channel Capital towards Climate-friendly projects.

8. REs could enhance transparency and disclose their alignment with UN PRI principles, Climate-related risks in portfolios, and engagement activities, fostering trust and accountability with stakeholders and advancing the global transition to a low-carbon economy.

III. CONCLUDING REMARKS:

As India prepares for Climate Change and Sustainable Finance, the RBI’s Draft Disclosure Framework balances Environmental impact, Financial regulation, and Internal control. Bridging the gap between Baseline and Enhanced disclosures is crucial, focusing on Transition Finance, Governance, and Investor confidence. Learning from International Best Practices is essential for Global leadership and Policy Advocacy. Aligning with IFRS 2 principles, the Framework should aim to integrate comprehensive disclosures on Climate-related Risks and Opportunities, supporting India’s transition to Climate and Sustainability compliance with a flexible approach. 



Sonal Verma leads the ESG Practice in the firm as a Partner and Global Leader – Markets & Strategy. With his crossroad working with business & laws – he brings advice & technology for effective change management in the journey of ESG. Sonal is well acclaimed for his work in regulatory & compliance programs over the last decade. He had in the past worked with 1800 plus clients in India and 61 other countries globally. He has worked with the top 3 unicorns and many Fortune 500 companies. His clients have been across different industries, viz. Automotive and OEMs, Pharma and Life Sciences, Manufacturing, Chemical Industry, BFSI, Infrastructure and Utilities (including stateowned PSUs), e-Commerce and Fintech Companies, Diversified Conglomerates etc.



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¹Draft Disclosure framework on Climate-related Financial Risks, 2024, RBI, February 28 2024, <https://rbidocs.rbi.org.in/rdocs/Content/PDFs/DRAFTDISCLOSURECLIMATERELATEDFINANCIALRISKS20249FBE3A566E7F487EBF9974642E6CCDB1.PDF>.

²The Discussion Paper on Climate Risk and Sustainable Finance, RBI, July 27 2022, https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/CLIMATE_RISK46CEE62999A4424BB731066765009961.PDF

³TCFD has been disbanded since October 2023 and FSB has asked the IFRS Foundation to take over the monitoring of Companies.

⁴Draft Disclosure framework on Climate-related Financial Risks, 2024, RBI, February 28 2024, <https://rbidocs.rbi.org.in/rdocs/Content/PDFs/DRAFTDISCLOSURECLIMATERELATEDFINANCIALRISKS20249FBE3A566E7F487EBF9974642E6CCDB1.PDF>.