THE INVESTMENT ASSOCIATION

Response to the Taskforce for Nature-related Financial Disclosures Draft Disclosure Framework

About the Investment Association

The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 270 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £10 trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. 46% of this is for overseas clients. The UK asset management industry is the largest in Europe and the second largest globally.

Executive summary

The Investment Association and its members welcome the opportunity to comment on the TNFD framework. Investors recognise that nature-related risk and opportunities are becoming an integral factor to investment risks and returns. More than half of global GDP is dependent on the natural world. The United Nations Intergovernmental Panel on Climate Change (IPCC) found in its 2022 report that nature strategies including ecosystem protection, restoration and improved farmland management are among the most cost-effective solutions to limit global warming to below 1.5°C and biodiversity loss has been identified as one of the top three most severe risks to economic value over the next 10 years, with over US $44 trillion of economic value generation dependent on nature. Despite this, today natural climate solutions receive less than 3% of all global climate finance.

Asset managers are typically both users of sustainability-related data (which inform investment and stewardship decisions but are used for disclosures made to their clients) and are also responsible for preparing disclosures for their own shareholders and wider stakeholders. As a result of this, the asset management industry will need to understand how companies plan to adapt to nature-based imperatives as they transition to a sustainable economy, including through assessing transition risks and opportunities of investee companies that may impact long-term shareholder value. This largely relies on the provision of high quality, comparable and timely disclosures that are investor focused.

A lack of corporate disclosure requirements, assessment methodologies and corporate reporting standards have historically made it difficult for investors to understand their exposure to biodiversity risks across their portfolios. To this end, the TNFD framework is vital to investors to achieve their investment goals insofar as

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it facilitates decision-useful nature-related financial disclosures by entities on the risks and opportunities associated with biodiversity and nature, with the ultimate aim of supporting a shift in global financial flows in accordance with the need to conserve nature and towards nature-positive solutions. Encouragingly, some members are also extending proprietary systems to nature-related issues, which will allow for greater comparability of company performance to inform capital allocation decisions.

Members further value the global interoperability and harmonisation that TNFD has achieved with existing standards such as the Taskforce for Climate-related Financial Disclosures (TCFD), UK Transition Plan Taskforce Sector-Neutral Framework and the forthcoming International Sustainability Standards Board (ISSB) standards. This will be crucial to ensuring comparability and consistency in corporate disclosures, as well as providing preparers with a familiar basis on which to report. The framework also calls out the explicit interactions between climate change and biodiversity loss, and members agree that these risks should not be treated separately or sequentially. Better integrated reporting on both of these issues by corporates should be reflected within the company's strategy and business model and consequently any risk to long-term value should also be clear. In addition, integrated reporting helps to maintain a better oversight of the company's strategic narrative and prevents reporting from being siloed.

Most members recognise that biodiversity is a systemic risk which is core to long-term value creation. As such, a whole-of-ecosystem approach will be required to rapidly scale the deployment of capital for nature and in response to nature-related risks and opportunities. Alongside initiatives like the TNFD, some of our members have also joined coalitions and collective efforts such as the Science Based Targets for Nature (SBTN), the Natural Capital Investment Alliance and are signatories to the Finance for Biodiversity Pledge. This has also been supplemented through direct policy engagement with Governments and regulators. In the UK, it is evident that such efforts are coming to fruition as the Green Finance Strategy indicates the UK Government's intention to review the framework and assess its suitability for incorporation into UK policy and legislative architecture.

Our members have the following comments on the Draft Standard:

Integrated and interoperable disclosures are important for investors

Investors welcome the intended global interoperability of the TNFD framework, which will integrate on an ongoing basis the specific standards and disclosure requirements developed by the ISSB and builds upon the work by standards setters such as the Global Reporting Initiative and Sustainability Accounting Standards Board. Together with the direction adopted from the Global Biodiversity Framework (COP15) and the development of a global baseline for assurance of sustainability-related information, investors will have the necessary tools to integrate nature considerations into the investment process.

Members consider it prudent and of direct benefit to their roles as users and preparers of reports that the TNFD framework mirrors the four pillars of TCFD, which promotes ease of understanding for investors and preparers and may better enable preparers to move towards nature-integrated climate disclosures. This is important to investors for several reasons:

(i) The framework's general requirement 5*: "to integrate disclosures with other sustainability-related disclosures"* is important as integrating nature-related financial disclosures (NFDs) within the company's annual report and accounts promotes effective integration of these disclosures with the company's financing operations and business strategy. This will also be welcomed by those jurisdictions where TCFD reporting is already mandated, and will prevent siloed reporting that makes it harder for investors to follow the company's sustainability and strategic narrative.

(ii) Integration also has the additional benefit in the UK and elsewhere, that NFDs will appear in the annual report and accounts and are also thereby captured by the requirement for the company auditor to provide an opinion on the consistency of this information with the financial accounts and broader strategic narrative, introducing a layer of limited assurance that may be further enhanced as relevant assurance standards for sustainability-related information develop.

(iii) Integrated nature-climate disclosures also help to demonstrate the trade-offs and synergies between the two. For example, measures to protect and restore biodiversity, such as protecting forests and mangroves, also mitigate the effects of climate change by sequestering carbon. However, poorly planned reforestation (e.g. planting monocultures), while contributing to climate mitigation efforts, can harm biodiversity. Integrated disclosures, including intersections with the broader risk frameworks including social factors like human rights and interactions with native communities, will help preparers and users to better articulate a holistic approach to such trade-offs in ways that it is hoped will ultimately benefit nature, climate and communities.

However, there are currently concerns that have been raised by investors around companies failing to consider or disclose the impact of material climate-related matters when preparing their financial statements, with financial statements failing to reflect climate considerations in the companies' other reporting. Coherence in financial and sustainability reporting is key to investors and will continue to be with the forthcoming ISSB standards which recognise the connection between nature and climate and will make incremental enhancements to its Climate-related Disclosure Standards relating to natural ecosystems and will consider the work of the TNFD in helping to fulfil the information needs of investors. Where companies are expected to demonstrate consistency between financial information and nature-related disclosures, members note that further consideration should also be given to where companies should seek to make these disclosures. At present it is unclear whether this should be as part of the TCFD report, within a company's sustainability report or the broader annual report. As noted above, this will be important to prevent company reporting from becoming siloed. The TNFD may want to give this point further prominence as part of any accompanying guidance on disclosure recommendation 5.

Accommodating materiality approaches

IA members agree that nature and climate are inextricably linked and together represent a system-wide challenge with broad implications for the long-term value of investments. Many therefore consider addressing this challenge, including the kinds of trade-offs mentioned above, in the context of financial materiality, or 'single' materiality. We welcome that TNFD includes general requirement 1: "*preparers disclose their approach to materiality- aligning to external standards or regulatory requirements where appropriate- to help report users understand the context of the information being presented by the report preparer*". While financial materiality is and will remain central to the investment process and forms an important foundation for other sustainability-related disclosure frameworks, we recognise that some corporates have started to apply other materiality lenses when considering sustainability.

The TNFD proposes a flexible approach to materiality to accommodate the preferences and regulatory requirements of preparers and users across different jurisdictions. While the materiality approach of investors differs across the industry depending on their investment approach or client needs or expectations (and approaches are not mutually exclusive), as users of TNFD disclosures investors will all benefit from a clear understanding of a company's materiality approach. This is needed not only in broad terms but particularly how it has informed and shaped the wider set of TNFD disclosures including the LEAP approach. We recognise that preparers are unlikely to take a homogenous view in their approach to materiality, and the majority of our members welcome the flexibility afforded by the TNFD framework, provided that comparability across disclosures is not compromised and the approach to metrics is clear depending on the type of materiality a corporate chooses. Some members have further commented that disclosure of any materiality approach should focus on its application to the wider set of disclosures rather than a company's own interpretation of the needs of different stakeholders.

LEAP Framework and Scenario Analysis

Members support the use of LEAP which provides preparers with a clear and intuitive way to approach risk assessment. Some members note that having assessed the scenarios, attention should be given to an appropriate 'transition plan' and implementation of the plan- i.e. starting with the Prepare element of the LEAP approach which focuses on responding and reporting on nature-related risk and opportunities. Financial institutions that depend on other preparers from other sectors for their own disclosures may start with 'evaluate' (of the dependencies and impacts), particularly where company data on locations is not available. Further consideration could be given to what implications a transition plan has for changes in the entity's approach to management of nature-related dependencies and impacts. This will also need to align with the Transition Plan Taskforce's (TPT) Disclosure Framework.

We welcome the decision to produce a technical annex for scenario analysis and note that scenario analysis should help inform all phases of the LEAP approach. Scenario analysis can help:

(i) companies explore nature related risks and opportunities and management of these under plausible futures, and
(ii) help them to prepare and respond by testing the resilience of an organisation's strategic choices and response options to plausible futures.

As noted in the IA's 2023 Shareholder Priorities, as a starting point, investors would welcome greater disclosure on the process and governance of scenario analysis including:

- How climate scenario analysis impacts the company's business model and strategy; and

Any changes the board has made to the business model and strategy as a result of the outcomes of scenario analysis. Beyond this, we acknowledge that it would not be appropriate to apply a prescriptive approach to scenario analysis as this could stifle innovation particularly as quantitative approaches to scenario analysis continue to develop.

Scope of Disclosures

Our members welcome that the Framework has adopted the notion of Scopes to the nature context as 'direct' operations, 'upstream', 'downstream' and 'financed'. This reinforces the interplay with climate-related disclosures and should provide preparers with a familiar basis on which to report. Our members generally recognise that there is likely to be some complexity around scope 3 equivalent reporting for nature, given how location-specific nature-related issues are. As nature-related reporting will be new to many companies, we think it is right that firms start by prioritising specific activities or business lines where nature-related dependencies, impacts, risks and opportunities are more likely to materialise. For asset managers, we understand that this is likely to focus on certain asset classes or portions of financing activities. Our members would welcome further sector-specific clarificatory guidance on this in due course.

Engagement with Stakeholders

We welcome the technical guidance on stakeholder engagement which is now a general requirement within the TNFD framework. The LEAP framework further acts as a foundation to help engage with affected stakeholders, identify and assess actual and potential negative impacts, and address the harms to affected stakeholders within a company's value chain. Our members believe that engagement with stakeholders, including shareholders, should be an on-going business activity which is embedded into the wider organisational strategy and responses. Therefore, companies should have formally integrated organisational policies, process, and systems in place for the management of any significant issues that arise as a result of stakeholder engagement. For financial institutions, the Global Biodiversity Framework notes that stakeholder engagement should be applied throughout the life of financed activities and across the supply chain, and investors would benefit from the sector-specific guidance for financial institutions setting out what this means.

Value chain engagement can also be viewed as an opportunity, and in principle can make it easier for companies to develop new technology, collaborate with peers and stakeholders, share costs and execute projects that improve efficiency which helps to facilitate the transition to a nature-positive future. To this end, there will need to also be careful alignment with the disclosure recommendations on value chain engagement within the Transition Plan Taskforce's Disclosure Framework for transition plans.

Development of Nature-related Measures and Metrics and Guidance

Our members note that the complexity of biodiversity makes it difficult to measure, where unlike climate a common unit of measurement (tonne of CO2 equivalent) can be used to track and communicate its effects, no single metric will comprehensively capture all dependencies and impacts related to biodiversity. Some members will be familiar with certain metrics as advocated under the Global Biodiversity Framework (GBF), (e.g. Mean Species Abundance, Potentially Disappeared Fraction, Species Abatement and Restoration), and we are generally supportive of the framework not favouring a single metric. Financial institutions, given their reliance on others for underlying disclosure, will benefit from the scope to innovate in how they report on their portfolios. Some members have also noted that there could be a risk of financial institutions being pigeon-holed into using one methodology or data source to comply with standards and regulations until there is consensus on the best way to describe impacts and dependencies. As such the TNFD may want to set out a core set of metrics from the GBF as an appropriate starting point, to encourage disclosure on a 'comply or explain' basis, as appropriate to relevant sectors.

However, there is a concern that these metrics tilt heavily towards risks, whereas the TCFD framework generally achieved a better balance between risks and opportunities. This can reflect real-world conditions, which are not prone to produce such a balance, but there is value in the framework articulating the opportunities, including where today these are nascent or prospective e.g. a broader market for nature credits in which organisations may become providers and participants.

While it is positive that the framework draws on the Global Biodiversity Framework for consistency and sector-specific guidance, we note that it will only cover four priority sectors initially: financial institutions (including asset managers and owners), agriculture and food, mining and metals, and energy. We urge the TNFD to set out in broad terms its wider sectoral approach, focused on the material drivers in each sector, and provide guidance on the timings of further sector-specific coverage and any sector-specific considerations for preparers in the interim.

As a general usability point, while members are pleased to see the number of technical annexes and accompanying guidance to the framework, there is a view that the current on-line interactive platform is not particularly user friendly. We anticipate that the TNFD will publish a consolidated version of the framework in due course, however it should also consider a centralised approach to maintaining all the guidance documents in one place.