



SOUTH AFRICAN RESERVE BANK  
Prudential Authority

## **Policy Statistics and Industry Support Department**

### **FEEDBACK NOTE**

#### **Development of Guidance Notices for Climate-related disclosures, governance and risk practices for banks and insurers**

##### **Introduction**

1. This document details the process undertaken to finalise the Guidance Notices for climate-related disclosures, governance and risk practices for banks and insurers. It provides feedback on the consultation process and comments received. This feedback note is for informational purposes and may be useful for banks and insurers in their approach to climate-related disclosures, governance and risk management.

##### **Background**

2. The development of Guidance Notices for climate-related disclosures, governance and risk practices are part of the Prudential Authority's (PA) approach to incorporate climate-related risks in its regulatory and supervisory activities. These Guidance Notices follow on previous climate-related publications by the PA, including the 2019 Climate Disclosures and 2020 Climate Risks survey reports, the 2022 PA Communication on climate-related risks, and the PA engagements with selected institutions Board of Directors in 2023 on climate risks.
3. The draft Guidance Notices were published for public consultation in August 2023 to allow for inputs in the development process. Guidance Notices issued by the PA are not typically subjected to a public consultation process and usually published pursuant to a secondary regulatory instrument such as a Prudential Standard or Directive issued, or to provide Guidance on a particular regulatory or supervisory matter. The Guidance Notices on climate-related disclosures and governance and risk practices deviated in this instance from the standard approach. The nature and characteristics of climate-related risks, including the high level of uncertainty, longer time horizons and non-linear nature of climate effects, and the current limited but evolving data to predict future impacts necessitated this approach. The public consultation process permitted inputs in the development phase to ensure greater collaboration and a co-creative approach in recognition of the bespoke nature of climate related risk and its impact.

4. The Guidance Notices seek to provide coherence to evolving practices, promote comparative transparency and ensure appropriate international alignment in climate-related risk practices, governance, and disclosures. The Guidance Notices seek to enhance industry initiatives to deepen current climate-related governance and risk practices and disclosures on a voluntary basis.

## **Development Process**

5. The draft Guidance Notices were published for public consultation in August 2023. Industry engagements were held virtually, through the industry associations. A total of 45 written submissions were received on the four Guidance Notices from 28 entities, including industry associations. Bilateral engagements were held with the Financial Sector Conduct Authority (FSCA), and the Guidance Notices were shared and presented throughout the development process with the Intergovernmental Sustainable Finance Working Group (ISFWG) whose membership includes the South African Reserve Bank (SARB), FSCA, National Treasury, Department of Forestry, Fisheries and the Environment, and South African Revenue Services. The PA has also engaged with the International Sustainability Standards Board (ISSB), the Department of Trade, Industry and Competition and the Financial Reporting Standards Council on the potential adoption of ISSB in South Africa.
6. The PA contributes to international developments through active participation in the Basel Committee on Banking Supervision (BCBS), Task Force on Climate-Related Financial Risks (TCFR) and the International Association of Insurance Supervisors (IAIS) Climate risk steering group (CRSG), as well as the Financial Stability Board (FSB) Supervisory Review Committee, and the Network for Greening the Financial System (NGFS) supervision workstream. The work from these committees and networks is taken into consideration when developing domestic guidance and instruments.
7. The PA received comments requesting a combination of the two Guidance Notices- to cover both climate-related disclosures and governance and risk practices in a single note. Whilst the PA agrees that the topics are interrelated and could be combined, the preference at this juncture is to have two separate Guidance Notices to permit future updates of each topic independently. Both climate-related disclosures and governance and risk practices are evolving and iterative, with several factors affecting the pace of development and maturity.

## **Feedback on Comments Received**

8. Comments were received from various stakeholders, including financial sector industry associations, domestic and international financial institutions, environmental and other interested non-governmental and civil society organisations. Comments received were in response to the three questions the PA asked, and general comments. This document provides a high-level overview of the responses to the three specific questions asked and the

general comments submitted. These responses are intended to provide context and clarity into the changes and updates made in finalising the Guidance Notices.

9. The three questions asked were:
  - 1) Does the Guidance Notice provide an appropriate level of ambition?
  - 2) What are your current or major anticipated challenges to implementing the guidance?
  - 3) Whether there are any key areas the guidance notice does not cover?
10. For the Guidance Notices on climate-related disclosures, the responses indicated the level of ambition to be appropriate and reasonable. Concerns were raised on capacity to implement and thus responses were supportive of the incremental and iterative approach, and a differentiated or proportionate approach considering an institutions nature, size, and complexity. The responses were universal in supporting alignment with existing disclosure frameworks, particularly the ISSB. On metrics, the comments ranged from being too ambitious, to not being ambitious enough.
11. For the Guidance Notices on governance and risk practices, the responses found the level of ambition to be appropriate and reasonable. Concerns were raised on applicability and proportionality, which is covered further below.
12. For the Guidance Notices the key challenges provided were:
  - 12.1. Availability and access to credible, accurate and consistent climate data e.g., GHG (Greenhouse Gas) emissions data at client, sector, and asset level; region specific climate and economic variables;
  - 12.2. Scarcity of technical skills e.g., climate models and scenario analysis;
  - 12.3. Lack of sectoral classification standards, standardised time horizons and lack of standardised metrics;
  - 12.4. Quantification of climate opportunities;
  - 12.5. Implementation and coordination challenges given the pace, breadth, and depth of regulatory developments across jurisdictions; and
  - 12.6. Risk of disclosing sensitive information.
13. Some of the areas the Guidance Notices did not cover included exit lists, South African specific context including scenarios and transition pathways, references to just transition and biodiversity risks, guidance on stewardship, disclosure of how climate-related risks are included in investment policies, promotion of climate change opportunities to stimulate economic growth, promotion of nature-based solutions, climate competencies and conflicted Board members.
14. The PA took into consideration these challenges and additional areas in revising the Guidance Notices. The PA sought to achieve a balance by setting minimum expectations as a baseline from which to develop further requirements as resources and expertise improve. The PA is taking an iterative approach, cognisant that climate-related risks have unique features warranting specific focus but should ultimately be integrated into existing processes and frameworks.

Table 1: Summary of the responses to the questions the PA asked regarding the climate Guidance Notices

1. Level of ambition	2. Key Challenges	3. Additional areas
<ul style="list-style-type: none"> <li>• Appropriate and reasonable</li> <li>• Differentiated and proportionate approach</li> <li>• Alignment to ISSB</li> <li>• Challenges in scenario analysis and stress testing</li> </ul>	<ul style="list-style-type: none"> <li>• Access and availability of credible, accurate, consistent data</li> <li>• Skills and expertise, particularly for scenario analysis</li> <li>• Coordination with global developments</li> </ul>	<ul style="list-style-type: none"> <li>• South African specific scenarios</li> <li>• Biodiversity</li> <li>• Exit lists</li> <li>• Investment policies</li> <li>• Climate specific competencies</li> </ul>

15. The general comments received on the Guidance Notices can be categorised into the following categories:
- 15.1. Alignment with the ISSB: Most comments for the Guidance Notice on climate-related disclosures requested closer alignment to the ISSB standards.
  - 15.2. Technical clarity: There were comments requesting clarity on technical aspects of disclosures, governance and risk practices.
  - 15.3. Implementation: Numerous comments raised queries around implementation challenges and practicalities, including proportionality and applicability.

A summary of the key comments and responses for each of these categories is provided below.

16. On alignment to the ISSB, the Guidance Notices on climate-related disclosures were applauded for being aligned with the ISSB standard on climate disclosures as an international standard and baseline. Alignment to international standards was a unanimous request. Numerous comments requested closer alignment to the ISSB, including applying the scope and definition of materiality. The Guidance Notices were in many instances reworded and restructured to show the alignment with the ISSB. The content from the appendix was moved to the body of the Guidance Notice for clarity and duplications were removed. The core content in terms of the key information required to be disclosed, remained the same. Specifically, the key amendments and inputs to align the Guidance Notices with the ISSB were:
- 16.1. Materiality: The definition of materiality was included under the principles section, which was renamed to principles and conceptual foundations. This section was revised to align with the ISSB and remove any ambiguity. The materiality of the risk should be determined by the institution concerned in accordance with its individual risk appetite statement.
  - 16.2. Governance structure: The Guidance Notices continue to refer to the Board of Directors, as this is the most common governance structure in South African context. A footnote was included to note that the governance structure could be a board committee or equivalent body charged with governance.

- 16.3. Additional guidance: Where there was information in the draft Guidance Notices that were not included in the ISSB, these have been moved to a new section entitled additional considerations. This includes the recommendation for referencing the South African Green Finance Taxonomy, where appropriate, and incorporating South African specific elements in scenarios and stress tests. The comments on the difficulties in applying the green finance taxonomy are noted, and thus this recommendation is included as an additional consideration. The PA sought to achieve a balance between the challenges in applying the requirements and ensuring stakeholders are provided with consistent, comparable, and verifiable information. The PA is cognisant of greenwashing, and reporting on green assets and projects, both of which require a taxonomy to minimise risks.
- 16.4. Metrics and targets: The ISSB has metrics and targets which have not been included in the Guidance Notices. Comments received indicated there was scope to expand the quantitative metrics to align with ISSB requirements, and to ensure South Africa does not lag peer jurisdictions. Some additional metrics have been included, and other metrics included as additional considerations. These are included as additional considerations to consider the data challenges and various levels of maturity within the banking and insurance industry. The Guidance Notices are intended to be applied using a building blocks and iterative approach- starting with the core elements and then expanding to additional considerations over time, in proportion to the nature, scale and complexity of an institution.
17. The key amendments and responses to the comments on technical clarity regarding climate-related disclosures are as follows:
  - 17.1. Prescribe methodologies and time periods: There were comments received for the PA to be more prescriptive in methodologies and define time periods to be used. There were comments received that the requirements were too onerous and prescriptive. The PA has aligned with the ISSB requirements and sought to find an appropriate balance between prescribing methodologies, such as the GHG protocol, whilst allowing for some level of flexibility and proportionality so as not to be prescriptive and add unnecessary costs.
  - 17.2. Additional metrics: In general, the disclosure of emissions reporting was supported, noting the various challenges raised. Some commentators acknowledged that South Africa is lagging global peers particularly with regards to financed emissions disclosure. The ISSB cross-industry metrics have been considered and selected metrics included under additional considerations.
  - 17.3. Scenario expectations: Clarity was requested on what was meant by South African specific scenarios and if certain scenarios will be prescribed. At this stage, the PA is not prescribing scenarios nor has the PA undertaken supervisory climate scenarios to date. The Guidance Notices were amended to clarify that the guidance is to disclose how South African-specific context was considered in scenario analysis.
  - 17.4. Group and branch disclosure: The Guidance Notices have been amended to clarify disclosure at consolidated group level.
  - 17.5. Value chain reporting: The Guidance Notices are aligned with the ISSB in requiring institutions to disclose the impact of climate-related risks and

- opportunities on their business and value chain. Acknowledging the challenges in value chain reporting, the Guidance Notices provide for institutions to disclose to what extent and whether any parts of their value chain are included or excluded from its processes for identifying, assessing and managing climate-related risks and opportunities.
- 17.6. Reporting period: The updated Guidance Notices clarify the reporting is for the same period as the annual financial statements.
  - 17.7. Inclusion of sustainability, biodiversity, and other environmental risks: These Guidance Notices are likely to be iterative and start with climate-related risks. Other environmental risks and sustainability disclosures may be considered in future, where it is relevant to the PA's mandate.
18. The technical comments on the Guidance Notices on governance and risk practices requested specific guidance and prescriptive details. These requests ranged from specifying what would be considered acceptable evidence of Board oversight, to standardised risk metrics.
- 18.1. Governance: Some of the comments were not bespoke to climate-related risks and thus should be informed and guided by existing governance requirements and internal policies.
  - 18.2. International alignment: Guidance Notices by their nature are intended as guidance and not prescriptive regulatory instruments. The Guidance Notices are aligned to climate risk principles espoused by international standard setting bodies, particularly the BCBS and IAIS.
  - 18.3. Transition Plans: Transition planning is an important component of climate risk management. The inclusion of transition planning in the Guidance Notices is to signal this importance, and potential future requirements for supervisory engagements. Transition planning is acknowledged as a journey and work in progress, with numerous challenges around data and transition pathways. Thus, the Guidance Notices are not prescriptive of the form or disclosure of transition plans at this point in time. The guidance provided falls within the mandate of the PA to ensure the safety and soundness of financial institutions, noting the primary tools for mitigation and adaptation to climate change are vested with government departments.
  - 18.4. Capital adequacy: This section was amended to clarify that scenario analysis and stress testing can be used for numerous objectives, including risk management, and that stress testing should be sufficiently severe but plausible.
  - 18.5. Scenario analysis and stress testing: Many comments raised challenges in undertaking scenario analysis and stress testing, and the different objectives for such exercises. Many comments requested the PA be prescriptive of the scenarios to be applied and to clarify the expectation around quantifying internal capital requirements based on climate risk scenario analysis, and the timeline for implementation. The PA acknowledges the challenges with stress testing and scenario analysis. However, as these analyses will form an integral part of a robust forward-looking assessment process, there is a need to start the work and thinking which can be refined over time. The guidance does not describe the frameworks to be used or leveraged, thus institutions can decide to use or leverage existing international guidance (such as from the Network for Greening the Financial System) if this is appropriate in their context.



Similarly, for institutions that are part of a bigger group, leveraging group stress testing and scenario analysis may be considered appropriate. Ideally, the time horizon for climate-related risks should be longer than three years, however, three years is specified as a minimum. Institutions can start to explore what the impact would be for longer time horizons although they are still able to use three years.

- 18.6. Legal risk: the description and references to legal risks have been moved from the Compliance section to the section entitled Risk management function. This amendment was made in response to numerous comments on the specific nature of the Compliance function as distinct from the Legal function. To this end it was stated that the Compliance function oversees and monitors the institution legal and regulatory obligations whilst promoting and sustaining a sound compliance culture. Litigation risk on the other hand falls within the purview of the Legal function more specifically in the tracking and management of litigation risk. Climate litigation risk has therefore been carried to the Risk management function which is a better fit in terms of the ambit of the Risk management function.
19. Lastly, there were comments received requesting clarity on proportionality, applicability and implementation. These are applicable to all four of the Guidance Notices.
  - 19.1. Proportionality: Proportionality is an inherent principle to the PA's supervisory and regulatory frameworks. The principle of proportionality is incorporated in the Guidance Notices where relevant. This includes for example the concept of "without undue cost and effort" which has been included under the strategy section, and that climate scenario analysis should be commensurate with the institution's circumstances, including their skills, capabilities, and resources. If there are parts of the Guidance which are not applicable for example to linked insurers, this should be explained as part of the disclosure. Similarly, linked insurers and branches of foreign insurers should apply the guidance on governance and risk practices on a proportionate basis. Given this is a guidance notice and not a prudential standard, there is no need for a transition period or permanent relief from some of the requirements.
  - 19.2. Applicability: The guidance is applicable to multinationals reinsurers. Reinsurers are insurers albeit licensed to conduct a specific class of insurance business. The Guidance Notices are applicable to all licensed insurers in South Africa. The PA will have due regard to equivalency in its supervision of insurers and banks that are headquartered offshore. Disclosures of metrics and targets should be made at consolidated group level.
  - 19.3. Resources to support institutions: The ISSB has developed numerous application guidance, illustrative guidance, and illustrative examples which institutions should make use of. The PA will also look to provide illustrative examples as local practices evolve and mature. In addition, the BCBS and IAIS have published various climate risk management resources.
  - 19.4. There were numerous comments around implementation of the Guidance Notices- whether it would be phased and when would it become mandatory. The purpose of Guidance Notices is to provide guidance, they are not legally enforceable regulatory instruments. There is thus no need for a transition period. The PA intends following a graduated approach to the management of

climate-related risks by supervised institutions. Whilst not enforceable, the PA will through ongoing supervision monitor the implementation of these Guidance Notices.

- 19.5. Supervision: The PA has developed an internal supervisory guideline for supervisors which incorporates the guidance provided in these notices. Thus, supervisors will start to engage entities as part of their ongoing supervision practices on their implementation and progress with regards to these Guidance Notices. Supervisors will also solicit feedback and comments on challenges that institutions may face. Initially, the reliability of the data and disclosures will mostly be driven by internal governance and audit processes (i.e. no external audit requirements initially).
- 19.6. The Guidance Notices on climate-related disclosures clarify that mandatory disclosures would be reliant on numerous factors. Should South Africa adopt IFRS (International Financial Reporting Standards) S1 and S2, the PA may not need to issue additional guidance unless there are areas that these standards do not adequately cover, or additional requirements from international standard-setting bodies such as the BCBS and IAIS.
- 19.7. The Guidance Notices are for public disclosures, and not specifically for, but may inform regulatory returns. The PA is piloting a data template for climate risk indicators in 2024.

## **Conclusion and Next Steps**

20. It is important to progress the work on climate risk management and disclosures to ensure institutions and the financial system build resilience to the risks of climate change. The Guidance Notices provide the minimum expectations for institutions climate-related disclosures and governance and risk practices.
21. The PA will continue to engage in relevant discussions at international fora on how regulatory frameworks and supervisory practices need to be adjusted to account for climate risks.
22. The PA will consider over time other regulatory instruments, such as prudential standards, that require mandatory compliance. The PA will consider joint regulatory instruments with the FSCA within respective mandates.