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30 June 2020

Pengarah,
Jabatan Penyeliaan Konglomerat Kewangan,
Bank Negara Malaysia,
Jalan Dato' Onn
50480 Kuala Lumpur

By email: climatechange@bnm.gov.my

Dear Sir / Madam,

Bank Negara Malaysia - Climate Change and Principle-based Taxonomy Discussion Paper

CPA Australia represents the diverse interests of over 166,000 members working in 100 countries and regions around the world, including around 10,500 members in Malaysia. We make this submission on behalf of our members and in the broader public interest.

We commend Bank Negara Malaysia (BNM) on this initiative, which we note clearly reflects the recommendations outlined in 2019 by the Network for the Greening of the Finance System (NGFS). Both BNM and the Reserve Bank of Australia are members of this Network, along with many other central banks, plenary and observer members. It is valuable in the context of this submission to quote introductory observations from the *Executive summary* to NGFS's first comprehensive report (April 2019) *A call for action: Climate change as a source of financial risk:*

> *The legal mandates of central banks and financial supervisors vary throughout the NGFS membership, but they typically include responsibility for price stability, financial stability and the safety and soundness of financial institutions. Even though the primary responsibility for ensuring the success of the Paris Agreement rests with governments, it is up to central banks and supervisors to shape and deliver on their substantial role in addressing climate-related risks within the remit of their mandates*.

A range of policy and capacity building issues stem from these remarks, on which we elaborate below:

- The importance given by central banks and financial supervisors to the economic and market impacts of climate change
- The appropriate level of reference to the key international instrument for driving climate change mitigation and adaptation – the United Nations Framework Convention on Climate change (UNFCCC Paris Agreement)
- The critical importance of cross-agency collaboration
- Efforts towards coordinated capacity building within both the finance sector and the real economy.

Climate-risk in the execution of central bank mandates and actions of financial supervisors

NGFS has devised a structure of recommendations which we summarise as follows:

> **Recommendations 1 to 4** are aimed at inspiring central banks and supervisors - NGFS members and non-members – to integrate climate-related risks in financial stability monitoring, integrate sustainability issues more broadly into their own portfolio management and to, more broadly, bridge data gaps and build collaborations around intellectual capacity and technical assistance.
>
> **Recommendations 5 and 6** do not fall directly within the remit of central banks and supervisors, pointing instead to actions potentially taken by policymakers to facilitate the work of central banks.

For the purposes of this submission, **Recommendation 6** is the most pertinent, encouraging policymakers to support the development of a taxonomy of economic activities which:

- facilitate financial institutions' identification, assessment and management of climate and environment-related risk;
- help gain a better understanding of potential risk differentials between different types of assets; and
- mobilises capital for green and low-carbon investments consistent with the Paris Agreement.

In CPA Australia's view, there is a high level of interrelationship between: (i) the underlying policy objectives of greening the financial system, (ii) building capacity to manage climate-related and associated environmental risks, (iii) setting robust and adaptive criteria for evaluating the climate change impact, and (iv) determining the mitigation and adaption effects of economic activities.

This is demonstrated in the following table[1].

Priorities	Actions
1. The need to develop the tools and capacity for identifying climate risks relevant to financial business	BNM and Securities Commission Malaysia (SC) are collaborating with the World Bank to develop a principles-based taxonomy to enable financial institutions in Malaysia to classify green assets consistently
2. The need to develop a more complete understanding of the impact of climate-related risks to the Malaysian financial system and economy	BNM is actively involved in working together with the *Central Banks and Supervisors NGFS* to develop an analytical framework to assess such risks
3. The need to address the appropriate treatment of climate risks within the prudential and supervisory frameworks for financial institutions	As a start, BNM will require financial institutions to report their exposures to climate risks once work on the green taxonomy has been finalised. Information gathered through this process will be used by BNM to consider changes to prudential standards to better reflect risks from climate-related exposures.
4. The need for the central bank to strengthen the use of disclosures more broadly, to provide greater transparency on how climate risk considerations are integrated into business decisions	BNM will work with the industry to implement the recommendations of the FSB Task Force on Climate-related Financial Disclosures (TCFD) in Malaysia.
5. Financial industry will need to step forward and facilitate an orderly transition for households, businesses and	

[1] Key priorities identified by BNM in working towards building climate resilience and corresponding actions/activities initiated (per the Governor's Keynote Address at the Regional Conference on Climate Change on 25 September 2019) https://www.bnm.gov.my/index.php?ch=en_speech&pg=en_speech&ac=839

Priorities	Actions
governments to adapt to the physical and transition risks of climate change.	

In December 2019 the "Climate Change and Principle-based Taxonomy Discussion Paper" was issued to solicit feedback on the classification of assets associated with fund raising, lending and investment activities in a consistent manner, based on their exposure to climate risk. The acknowledged aims were to address the absence of agreed common definitions and data nationally, to enable the quantification of climate risk impacts on individual financial institutions and the broader financial system. It would also enable financial institutions to identify and expand similar opportunities, and to do so more confidently on a well-informed basis.

Furthermore, the BNM governor has said that financial institutions will be required to report their exposure to climate risks. The information gathered by the BNM could be used to set regulatory standards in Malaysia. She also noted that a new reporting requirement for financial institutions will kick in once classifications on green assets are finalised with the SC Malaysia and the World Bank.[2] Each of these initiatives or developments are consistent with measures underway in Australia, be it that they are at different stages of progress and have a different emphasis in application. Some of the measures in Australia are outlined below.

The Australian Prudential Regulation Authority (APRA), in a February 2020 bulletin to all APRA-regulated entities, stated:

> *APRA - - - continues to encourage the adoption of voluntary frameworks to assist entities with assessing, managing and disclosing their financial risks associated with climate change, such as the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) recommendations*.

And further,

> *Regulators and supervisors around the world are developing responses to the climate data deficit. In particular, the insights gained through climate-related scenario analysis are being considered, including through the Central Banks and Supervisors Network for Greening the Financial System (NGFS). Domestically, industry-led initiatives are considering taxonomy and scenario design questions to improve understanding of the financial risks of climate change and support strategic decision-making for all businesses.*
>
> *In collaboration with these international and local stakeholders, APRA will be seeking to undertake a climate change financial risk vulnerability assessment. The assessment will begin with Australia's largest authorised deposit-taking institutions (ADIs). Beginning with the ADI industry will provide helpful insights on the impact of a changing climate on the broader economy, which will be analysed in conjunction with the Reserve Bank of Australia (RBA). The ADI vulnerability assessment will be designed in 2020 and executed in 2021, with other industries to follow. This timing also aligns with the expected release of international peer regulator guidance on scenario analysis for the banking sector*.

What can be deduced from the current development trend in Australia is a greater emphasis on data derived through use of the TCFD Recommendations (in some ways reflective of NGFS recommendation 3) and a 'lighter touch' with respect to driving finance market participants towards building climate change-sensitive portfolio management. This is not an indication that taxonomic analysis of economic activity is not a feature of finance market and participant transformation. Indeed, this a cornerstone of collaborative arrangements currently underway with the Australian Sustainable Finance Initiative (ASFI)[3]. Significantly, both the BNM proposal and ASFI make reference to, and draw from, the EU Technical Export Group on Sustainable Finance and its evolving taxonomy development. More generally, neither of the Malaysian or the Australian approaches or orientation is necessarily superior to the other. Rather, what CPA Australia urges, is an awareness of the trends in approach which may over

[2] https://bursasustain.bursamalaysia.com/droplet-details/news/malaysia-to-require-banks-to-report-exposure-to-climate-risks
[3] https://www.sustainablefinance.org.au/

time converge, recognising that the subject matter of climate change mitigation and adaption is both rapidly evolving and highly complex.

Reference to the international climate change policy architecture

CPA Australia notes the remarks, made in the introduction to this Discussion Paper, of Malaysia being a signatory to the Paris Agreement and its commitment in the form of an Intended Nationally Determined Contribution (INDC). To a substantial degree, national policy must work within this evolving international collaborative framework. The BNM's proposed principle-based taxonomy provides ample recognition of this critical framework for addressing the human, environmental and economic effects of global warming.

We make a number of observations about trends in climate change policy, particularly as these may influence the application and future development of BNM's Taxonomy.

The science, politics and economics of climate change and sustainable development have long dealt with the controversy about the relative merits and efficacy of adaptation versus mitigation policies. The consensus which has emerged over at least three decades of debate is that an integrated portfolio involving both trying to avoid greenhouse gas emissions (mitigation), whilst at the same time working towards coping with the impact of global warming (adaptation), is essential. In these terms, BNM's Taxonomy, at Guiding Principles 1 and 2, reflects this vital duality in policy approach. As the Discussion Paper notes in relation to GP1 "*reduction of emissions can be performed via several mechanisms, such increasing energy efficiency, use of renewable forms of energy and carbon capture and storage technology*." CPA Australia is of the view that this points to the reality that the United Nations Framework Convention on Climate Change's target of limiting global warming cannot be met through the trajectory of emissions reduction, even at highly ambitious levels. Correspondingly, the technological path has profound implications for governments' fiscal policy, which CPA Australia urges should be a factor which will shape how BNM monitors and adapts the Taxonomy to evolving climate-related economic circumstances. One potentially useful source of insight around policy development in this area is the Australian Government's Technology Investment Roadmap *A framework to accelerate low emissions technology.*[4]

Finally, we note the character of nationally determined contributions (NDCs as the more formal incremental development from an INDC) as the primary articulation of a signatories' pathway on net carbon emissions reduction. Ideally, these provide a clear long-term signal, depending upon a nation's stage of economic development, of the stages towards reaching net-zero emissions in the 2050 – 2100 timeframe. Within this, the imposed five-year interval 'review, refine and rachet' mechanism can provide national regulators a basis for communicating through its oversight and intervention processes—in BNM's case its proposed Taxonomy—the expected trajectory of economic transitioning.

Cross-agency collaboration

The aforementioned APRA bulletin notes that:

> *APRA has, supported by other agencies of the Council of Financial Regulators, sought to ensure regulated entities are actively seeking to understand and manage the financial risks of a changing climate just as they would other economic and operational risks*.

And further,

> *APRA will coordinate this work with the Australian Securities and Investment Commission (ASIC) and the RBA [Reserve Bank of Australia] via the Council of Financial Regulators to ensure consistency in the application of scenario analysis, disclosure recommendations and to analyse the macroeconomic impacts of climate change*.

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[4] https://consult.industry.gov.au/climate-change/technology-investment-roadmap/supporting_documents/technologyinvestmentroadmapdiscussionpaper.pdf

These words clearly identify the reality that driving both the financial and real economy towards low emissions and environmentally sustainable outcomes requires multi-agency collaborative effort.

CPA Australia has conducted a short 'survey' of local initiatives, many of which BNM will be familiar with, which points to existing institutional capacity which we believe can be built upon to ensure that implementation and application of the Taxonomy is given optimum opportunity for effect. These are summaries in the attached Appendix reiterating our view that addressing the challenges of climate change is a 'whole of government' responsibility and in which capacity building across the economy, and within this the business sector in particular, should be a major driver.

Efforts towards coordinated capacity building within both the finance sector and the real economy

In terms of the role of related policy initiatives and pronouncements, CPA Australia highlights an August 2019 update to ASIC's Regulatory Guide (RG 247) for preparation of the operating and financial review by listed company directors.[5] This update in addressing prospects for future financial years now provides an emphasis that "*climate change is a systemic risk that could have a material impact on the future financial position, performance or prospects of entities*."[6] Within this, direct mention is made of the TCFD. Similarly, the 2019, 4th Edition, of the Australian Stock Exchange's Corporate Governance Principles and Recommendations have been strengthened to give greater guidance around materials and references relevant to disclosing the presence and processes for managing environmental risks. Again, reference is made to the TCFD. Finally, another Australian regulatory development is the joint bulletin from the Australian Accounting Standards Board and the Auditing and Assurance Standards Board: *Climate-related and other emerging risk disclosures: Assessing financial statement materiality using AASB/IASB Practice Statement 2*. Aside from the reference again to the TCFD, this Practice Statement is highly significant with respect to its criteria for application, including investor expectations that climate-related risks could influence their decisions.

These instruments or mechanisms of public policy have economy-wide application beyond the finance sector and the policy remit of central banks and financial supervisors. However, CPA Australia highlights these developments as relevant to BNM's current Taxonomy initiative and wider climate change-related oversight and supervisory activities in the following ways:

- The financial stability and transparency gains being sought will likely be undermined if associated capacity within the wider economy is not developed, around collection, assimilation and presentation of relevant data, along with the capacity to adjust practice and wider business models in response to climate change-related risks and opportunities.
- Across many, if not all, nations, these capacities are presently in a state of development, particularly at sector and economy-wide levels – this notwithstanding the rapidly growing sophistication and rigour of non-financial disclosure frameworks.
- Respective financial and non-financial responses to climate change mitigation and adaptation should be drawn from a common understanding of the economic transformation implications.

CPA Australia sees that the BNM's taxonomy development will play a key role with respect to the third dot point above.

[5] Corporations Act 2001 section 299A
[6] RG 247.66

If you have any queries, please do not hesitate to contact Dr. John Purcell, Policy Adviser ESG at CPA Australia on john.purcell@cpaaustralia.com.au or +613 9606 9826.

Yours Sincerely,

Priya Terumalay FCPA (Aust.)	**Dr. Gary Pflugrath CPA (Aust.)**
Country Head – Malaysia	**Executive General Manager, Policy and Advocacy**

Encl.

APPENDIX

BNM and SC established the Joint Committee on Climate Change (JC3) to drive and coordinate the financial industry's collective response to climate risks.[7] Formed in September 2019 the JC3 is intended to pursue collaborative actions to build climate resilience within the Malaysia financial sector. It is co-chaired by Deputy Governor of BNM and Deputy Chief Executive of the SC[8]. Its mandate is:

- building capacity through sharing of knowledge, expertise and best practices in assessing and managing climate-related risks;
- identifying issues, challenges and priorities facing the financial sector in managing the transition towards a low carbon economy; and
- facilitating collaboration between stakeholders in advancing coordinated solutions to address arising challenges and issues.

The JC3 recognised the urgent need to accelerate responses towards ensuring a smooth and orderly transition to a low-carbon economy. This includes managing exposures to climate risks and facilitating businesses to transition towards sustainable practices. To take this forward, four sub-committees were formed, focusing on:

- risk management;
- governance and disclosure;
- product and innovation; and
- engagement and capacity building

The BNM is also part of the Malaysian Green Financing Taskforce, chaired by SC Malaysia, to spur private sector financing in the renewable energy sector. [9]

The SC launched a Sustainable and Responsible Investment (SRI) Roadmap for the Malaysian Capital Market in 2019. The Roadmap is used for charting the role of the capital market in driving Malaysia's sustainable development.[10]

Bursa Malaysia[11] –

"Sustainability Reporting Guide and Toolkits – 2nd Edition Guide and Toolkits" - updated in 2018 is based on TCFD recommendations to encourage listed issuers to assess and disclose material climate-related information in their annual reporting. In the first edition issued in 2015, assistance was provided for listed issuers in the preparation of a sustainability statement and embed sustainability practice within their businesses. The 2nd Edition Guide and Toolkits incorporated refined guidance on materiality assessment, updated case studies and example disclosures to provide the latest best practices for listed issuers to consider. In addition, the United Nations Sustainable Development Goals are included to assist listed issuers in making impactful contributions to the goals through strategic implementation and disclosure.

Companies Commission Malaysia (SSM)[12] –

Referring to a 2017 circular, companies and corporations are encouraged to adopt a variety of voluntary corporate responsibility initiatives, such as:

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[7] https://www.businesstoday.com.my/2020/04/03/bank-negara-urges-financial-institutions-to-treat-climate-risk-like-any-other-financial-risk/
[8] https://www.bnm.gov.my/index.php?ch=en_press&pg=en_press&ac=4920
[9] ibid
[10] https://www.sc.com.my/api/documentms/download.ashx?id=a0099ceb-8908-44d3-9399-950e83d86f53
[11] https://www.bursamalaysia.com/about_bursa/media_centre/bursa-malaysia-reinforces-support-of-tcfd-recommendations-in-updated-sustainability-reporting-guide-and-toolkits
[12] https://www.ssm.com.my/Pages/CR/Document/best_business_practice_circular_6-2017.pdf

- codes of conduct on measures to improve environmental management systems and occupational health and safety;
- company 'triple bottom line' reporting on financial, social and environmental aspects;
- participation in certification and labelling schemes;
- dialogue with stakeholders and partnerships with NGOs; and
- increase support for community development projects and programs with the public and stakeholders by conducting awareness programmes.

Further within the formal remit of SSM, the content of the business review prepared under Companies Act 2016 section 253 (Fifth Schedule Part II) may contain information about environmental matters (item 2(d)(i)) to the extent necessary to enable an understanding of the development, performance and position of the company. This has been extended to include disclosures which "measure the direct benefit and risks of climate change which affect the company's credibility in the market."