Federico Cellurale
Financial Conduct Authority
12 Endeavour Square
London, E20 1JN

By email: cp20-03@fca.org.uk

1 October 2020

Dear Mr Cellurale,

Re: BVCA response to FCA Consultation Paper 20/3 on proposals to enhance climate-related disclosures by listed issuers and clarifications of existing disclosure obligations (the "Consultation Paper")

We are writing on behalf of the British Private Equity and Venture Capital Association (BVCA), the industry body and public policy advocate for the venture capital and private equity industry in the UK. We represent the vast majority of all UK-based firms (over 700), as well as their professional advisers and investors. The BVCA represents the vast majority of all UK based PE/VC firms, as well as their professional investors and advisers. Over the five-year period 2014-2018, BVCA members invested over £38bn into nearly 2,800 companies based in the UK. Our members currently back around 4,330 companies, employing close to 1.6 million people on across the world, including 843,000 in the UK.

Why this Consultation Paper matters to PE/VC firms

ESG factors are important to many BVCA members who seek to minimise risks and create value in their own businesses, and in the underlying portfolio companies held by the investment vehicles that they manage or advise, in order to enhance returns for investors. Those investors include insurance companies, pension funds, development finance institutions, charitable foundations and other institutional investors.

Our membership includes firms that focus on providing a range of financial, social and environmental returns to investors in varying combinations, including firms that focus on financial returns through climate change related strategies (such as resource or energy efficiency). Many have adopted and report under existing ESG related initiatives (a significant number are signatories to UN PRI) or provide bespoke ESG reporting (particularly environmental) to investors. UN PRI members have been able to report on TCFD-aligned indicators since 2018 as part of the PRI reporting framework and from March 2020 it became mandatory to report on indicators relating to governance and strategy (although public disclosure remains voluntary).

These developments demonstrate that climate change, mitigating related risks, and the transition to a low carbon economy are prominent issues for BVCA members and investors in PE/VC funds.

Most PE/VC funds are structured as private limited partnerships that invest in private companies, and so the proposals in the Consultation Paper are not directly applicable to the majority of our membership's business activity. However, the changes may affect our members for the following reasons:

1. The BVCA's membership includes a small number of publicly listed firms which may be within the scope of the new rule in their capacity as listed issuers (rather than as regulated firms) and for whom the Technical Note would be relevant.

2. Some BVCA members may choose to voluntarily comply with the TCFD asset manager framework.

3. TCFD disclosures may be indirectly relevant because of commercial interaction with an in-scope issuer. A significant proportion of PE/VC firms engage in transactions relating to companies with publicly listed securities (from buyer, seller and issuer perspectives), including from portfolio company exits through initial public offerings, take-private transactions, and portfolio company level mergers and acquisitions involving publicly listed companies.

We therefore welcome the opportunity to respond to the Consultation Paper.

Overall comments and key points

We note that the FCA is considering how to enhance climate disclosures from regulated firms including the broader population of asset managers, and welcome your commitment to coordinating with Government and other regulators, taking into account interactions with the developing EU disclosure frameworks. That element of the FCA's approach to climate and broader sustainability regulation constitutes an important workstream for BVCA member firms, which typically operate UK or EU regulated entities (or both) and have also been closely following EU developments in this space. We look forward to engaging with you as you develop this approach in due course.

In the meantime, we would like to make the following points in relation to the Consultation Paper:

- *Importance to PE/VC firms of generic disclosures from listed issuers*: The majority of BVCA members are private equity and venture capital fund managers that are users of non-financial information relating to companies they invest in (which are principally unlisted companies). PE/VC fund managers are currently able to specify and obtain the non-financial information they require from investee companies, either for regulatory reasons or to satisfy the needs of fund investors, in greater detail and in areas more suitable to their and their own investors' needs than would likely be provided by standardised public disclosures. This is a direct consequence of the exchange of information during negotiations in the acquisition process and the very close relationship between PE/VC investors and portfolio companies. Against that background, it is unclear how many of our member firms would benefit directly as investors from any mandating of further public, climate-related disclosures from the companies they invest in, particularly as portfolios change regularly as funds invest in and divest from companies with varying holding periods, making useful year-on-year comparisons very difficult without providing a disproportionate amounts of information.

- *Proportionality*: The BVCA supports the FCA's proportionate approach to measures to support price discovery in the public markets and transparency in relation to climate risk, and competition and innovation in relation to green finance. We firmly support the points made by the FCA in the Consultation Paper that any regulatory intervention should be proportionate, efficient and cost-effective, should not stifle positive innovation, and should support the UK's position as an attractive prospect for international business and finance and the UK's competitiveness as a hub for green finance. Adoption of the TCFD recommendations on a "comply or explain" basis for premium listed issuers, as proposed by the FCA in the Consultation Paper, seems proportionate.

- *Capabilities*: Firms may not yet have the capability to comply with the proposed rule, as is referred to in paragraph 1.8. Potential moves in the future to extend the requirement further to include private companies/fund managers may present significant issues, particularly if the obligation changes from being 'comply or explain' to 'comply', as there could be extra challenges with obtaining the data necessary to comply depending on the asset class/geography of their products. For example, a midsize emerging markets fund manager may find it impossible to obtain detailed climate data from portfolio companies based in jurisdictions that are significantly further behind the curve in terms of ESG legislation/regulation. Another example might be a distressed debt fund that would likely have limited access to detailed climate data on the underlying companies in its portfolio. Overall, the practical challenge that would be faced by fund managers in obtaining reliable data should not be underestimated.

- *Materiality*: The determination of materiality is issuer and situation specific, and varies considerably by factors including geography, industry, sector, supply chain, and exposure to natural resources, so a flexible approach is required.

- *Duplication and consistency with other requirements*: The obligation on climate risk disclosures should not duplicate other obligations to which firms may be or become subject (in particular, the EU's proposals on sustainability disclosures under SFDR), which is less likely to occur if the obligation is on a principles or outcome basis. Overall, the objectives should be to ensure: (i) a coherent framework; and (ii) that there is consistency between the various frameworks/requirements to avoid inefficiencies, inconsistencies and disproportionate resource burden on companies. Flexibility is particularly important for the PE/VC industry given the diversity of investment strategies it encompasses. However, if there is ambition to head towards a unified framework, then we would strongly encourage consistency and advocate for a coherent regulatory approach to climate related and broader ESG disclosures.

- *Distorting the market*: Any regulatory obligation or guidance specific to climate risk should not distort markets, for example by making disclosures relating to the risks and opportunities resulting from climate change more prominent than their relative importance would justify for certain issuers for whom climate risk is a low order risk relative to other risks (for example, market, credit or counterparty risk).

- *Conflict with financial promotion rules*: In our response to FCA DP 18/8 we noted that any obligation on firms to make climate risk summary information public should not conflict with a firm's obligations under the UK and other relevant financial promotion and marketing regimes, e.g. exposing firms to the risk that they may be required to make fund information public which could be regarded as breaching marketing restrictions in certain jurisdictions. This will be particularly important to PE/VC fund managers with global investor bases as the FCA's approach to regulated firms is developed.

- *Clarity around the scope of the disclosures*: There should be further efforts to clarify the scope of the proposals. The Consultation Paper refers both to the climate-specific TCFD recommendations and the proposed draft Technical Note, which encourages issuers to consider broader ESG issues than just climate-related disclosures. The latter is also relevant to all issuers and not just those with a premium listing. There is a risk of confusion, especially as to the scope, given that the proposals are within the same document.

- *Directors liability*: Directors of the issuer may have liability concerns with respect to public disclosures, referred to in paragraph 4.56, particularly in relation to forward-looking statements. Potential solutions should be sought to alleviate these concerns.

Responses to consultation questions

We have responded to the questions in the consultation most relevant to PE/VC funds.

Q1. Do you agree that our new rule should apply only to commercial companies with a premium listing, at least initially? If not, what alternative scope would you consider to be appropriate, and why?

Yes. We agree with this approach. However, we do have a concern that non-listed issuers may at some point find themselves subject to the rule, or some version of it, that may prove disproportionate, for smaller issuers in particular.

Q2. Do you agree that sovereign-controlled commercial companies with a premium listing should also be in scope? If not, why should these companies not be included?

Yes. We think it is important to maintain "a level playing field" , to assist comparison between listed companies, irrespective of ownership.

Q3. Do you agree with our approach?

We note that the FCA is considering how to enhance climate disclosures from regulated firms including the broader population of asset managers, and welcome your commitment to coordinating with Government and other regulators, taking into account interactions with the developing EU disclosure frameworks. That element of the FCA's approach to climate and broader sustainability regulation constitutes an important workstream for BVCA member firms, which typically operate UK or EU regulated entities (or both) and have also been closely following EU developments in this space. We look forward to engaging with you as you develop this approach in due course.

We have particular concerns about the disproportionate impact on smaller PE/VC firms if they were required to disclose against the TCFD recommendations, given the practical problems they would face, particularly around the availability of data relating to SMEs, and their internal resources.

Q4. Do you agree that our rule should reference the 4 recommendations and 11 supporting recommended disclosures included in the TCFD's June 2017 final report? If not, what alternative approach would you prefer, and why?

Yes. The TCFD recommendations are a widely-accepted framework, recognised globally and therefore likely to help conform climate related disclosures and ensure consistency.

Q5. Do you agree that we should make explicit reference in Handbook guidance to the TCFD's "guidance for all sectors" as well as the "supplemental guidance for the financial sector" and the "supplemental guidance for non-financial groups" accompanying each recommended disclosure? If not, what alternative approach would you prefer, and why?

No comment.

Q6. Do you agree that we should include additional guidance which references the wider set of materials that have been published both within and alongside the TCFD's final report, as useful sources of guidance and interpretation when complying with our proposed rule?

No comment.

Q7. Do you agree that we should introduce the new rule on a 'comply or explain' basis? If not, what alternative approach would you prefer, and why?

Yes. Given the varying relevance of climate risks to issuers, any climate risk specific disclosure obligation on issuers should be on a “comply or explain” basis.

Q8. Do you agree that the recommended disclosures under the "governance" and "risk management" recommendations should not be subject to a materiality assessment? If not, what alternative approach would you prefer, and why?

Yes, as distinct from “risk and metrics” and “strategy” disclosures, which should always remain subject to materiality to avoid firms being forced to embark on a meaningless and potentially disproportionately costly box-ticking exercise.

Q9. Do you agree that issuers should ordinarily be able to make the recommended disclosures under the "governance" and "risk management" recommendations?

No comment.

Q10. Do you agree that no explicit guidance is needed to clarify that it would be acceptable for an issuer to explain non-disclosure of these recommended disclosures only on an exceptional basis?

No comment.

Q11. Do you agree that the statement of compliance and the proposed disclosures should be made within an issuer's annual financial report? If not, what alternative approach would you prefer and why?

We agree that the statement of compliance with the new proposed rule should be made within an issuer’s annual financial report but we would welcome greater flexibility around the location of the disclosures and, in particular, would recommend that firms have the ability to cross-refer to previous annual reports or sustainability reports.

Q12. Do you agree that an issuer should be required to include within the statement of compliance a description of where in its annual financial report (or other relevant document) its TCFD-aligned disclosures can be found? If not, what alternative approach would you prefer and why?

Yes.

Q13. Do you agree that the FCA should not require third-party assurance of issuers' climate-related disclosures at this time? More generally, we welcome views on the role of assurance for climate-related disclosures.

Yes. Notwithstanding the fact that there are requirements as to review by auditors of certain non-financial disclosures by listed companies, we would be very concerned about any possible assurance or inclusion of non-financial information within the scope of a company audit requirements without a clear understanding of the possible cost, which is likely to be disproportionate, for SMEs in particular. Audited financial information is clearly necessary for lenders/other counterparties, e.g. suppliers who place reliance on it before taking financial decisions and engaging in commercial activity with the company. This is not the case to the same extent for non-financial information, which also requires other expertise in many areas beyond finance and accounting.

Q14. Do you have any feedback on the interactions between our proposed rule and the role of sponsors in assisting premium listed issuers?

No comment.

Q15. Do you have any other feedback related to the interaction between our proposed rule and existing legislative and regulatory requirements and industry standards and practice?

No specific comments. However, in relation especially to any rules applicable in future to the broader population of regulated firms, we would like to stress the imperative of avoiding inconsistencies and overlaps between existing and proposed requirements. For example, although there appears to be no direct conflict with SFDR as it currently stands, there are potentially inconsistencies (depending on the final detail of level 2 measures) that would affect the many firms that will have to comply with both UK and EU rules, either because they have regulated entities in both jurisdictions or because they market to EU-based investors from the UK. For example, SFDR may require firms that opt in to principal adverse impact disclosures (or that are too large to opt out) to report various portfolio-wide metrics, including GHG emissions and weighted average carbon intensity. This seems consistent with the TCFD requirements relating to metrics. Equally, TCFD seems to go further than SFDR as regards reporting on climate change issues generally. Inconsistencies like these would unnecessarily increase both costs (for both firms and investors) and the potential for confusion.

Q16. Do you consider that our proposals adequately address the challenges, risks and unintended consequences described above? If not, what additional measures would you suggest?

On the whole, the 'comply or explain' basis is appropriate because it allows firms to explain any non-compliance (e.g. due to lack of available data, which is a significant practical concern) rather than having to state whether they comply in a yes/no fashion, which could ultimately be mis-leading to investors by giving them the impression that the entity is entirely non-compliant.

However, directors of an issuer may have liability concerns with respect to public disclosures, referred to in paragraph 4.56, particularly in relation to forward-looking statements. Potential solutions should be sought to alleviate these concerns.

Q17. Do you agree that our new rule should take effect for accounting periods beginning on or after 1 January 2021? If you consider that we should set a different timeframe, please explain why

No comment.

Q18. Do you agree with the conclusion and analysis set out in our cost benefit analysis (annex 2)?

No comment.

Q19. Do you agree with the guidance provided in the draft Technical Note set out in Appendix 2? Are there any changes that you would suggest? If so, please describe.

We would support further efforts to clarify the scope of the proposals. The Consultation Paper refers both to the climate-specific TCFD recommendations and the proposed draft Technical Note, which encourages issuers to consider broader ESG issues than just climate-related disclosures. The latter is also relevant to all issuers and not just those with a premium listing. There is a risk of confusion, especially as to the scope, given that the proposals are within the same document.

We would be happy to discuss the contents of this letter with you; please contact Tom Taylor (ttaylor@bvca.co.uk).

Yours sincerely,

Tim Lewis
Chair, BVCA Regulatory Committee