ESG standards, guidelines, frameworks and more: Breaking down what all this means for Canadian insurers

Environmental, social and governance (ESG) factors have quickly risen to prominence in the financial sector, reflecting mounting climate risks, rising stakeholder concerns and enhanced regulator expectations. In conjunction, there has been a rapid growth in ESG frameworks, standards and reporting requirements, making it difficult to unpack what's relevant to a given company.

This article will discuss the complexity of the ESG regulatory compliance landscape by summarizing the evolution of reporting standards and providing an overview of the relevant requirements impacting Canadian insurance companies.

The International Sustainability Standards Board (ISSB)

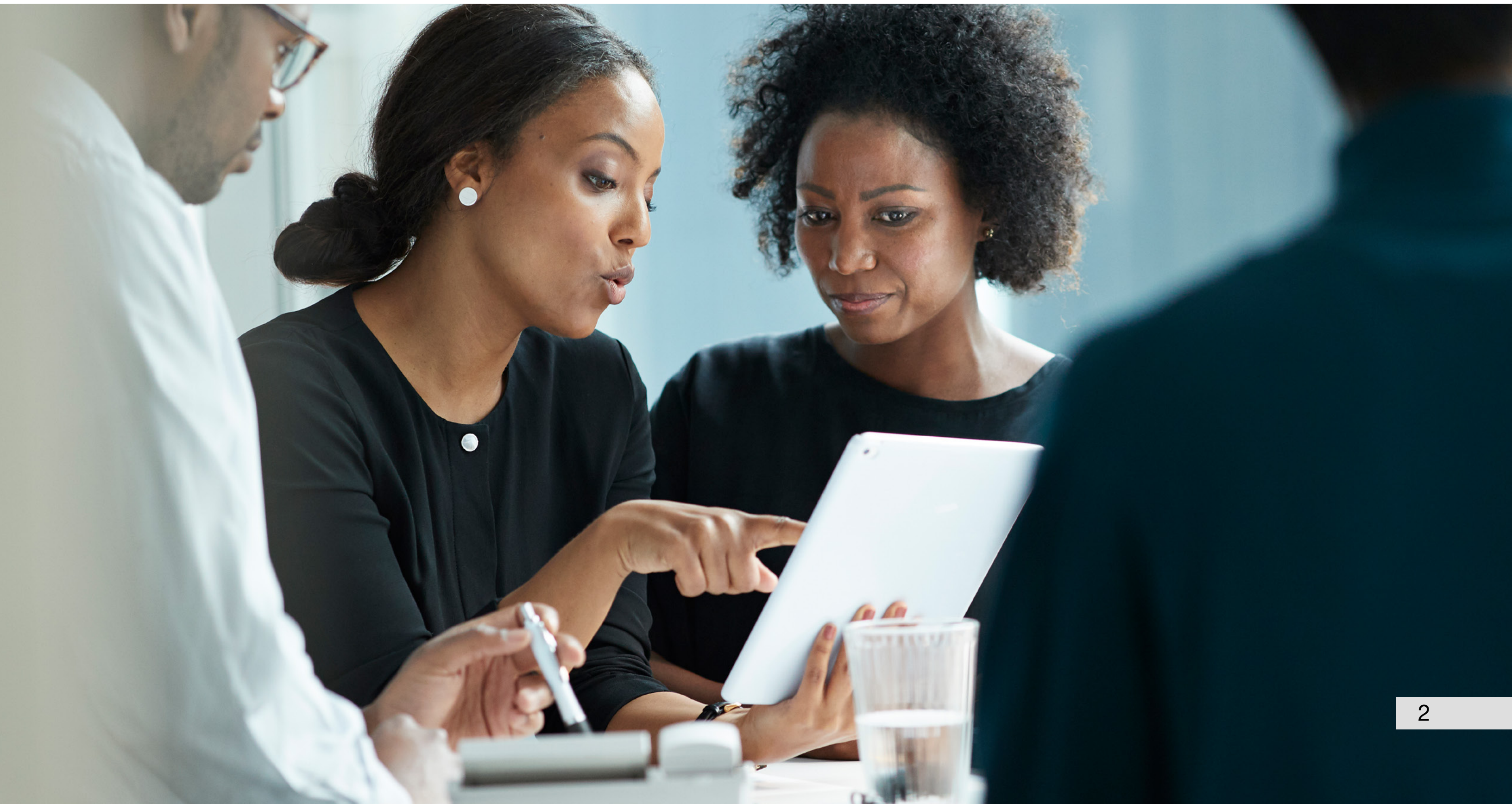
Most readers will be familiar with one or all of the following frameworks and standards: Global Reporting Initiative (GRI), the Task Force on Climate-related Financial Disclosures (TCFD) and the Sustainability Accounting Standards Board (SASB).

Building upon these frameworks, the International Sustainability Standards Board (ISSB) was introduced as a step towards consolidating and harmonizing global ESG reporting standards.

In June 2023, the ISSB issued its inaugural standards: IFRS S1 (general) and IFRS S2 (climate-related). The IFRS standards follow the TCFD recommendations and are structured in four content areas: governance, strategy, risk management, metrics and targets. While these current standards are currently voluntary, there are varying degrees of alignment and/or adoption by the regulators described in this article further below.

Looking forward, the ISSB will be starting projects that may support potential disclosures of risks and opportunities associated with biodiversity, ecosystems, ecosystem services and human capital.[1] The development of associated standards could impact the reporting requirements determined by other parties given the influence of the ISSB.

1 https://www.ifrs.org/news-and-events/news/2024/04/issb-commence-research-projects-risks-opportunities-nature-human-capital



The Office of the Superintendent of Financial Institutions (OSFI)

Climate-related financial disclosures

OSFI first published Guideline B-15 in March 2023, which focuses on climate risk management for all Canadian federally regulated financial institutions (FRFIs), including insurance companies. Updates were made in March 2024 to align with the ISSB's final IFRS S2 climate-related disclosures standard.[2]

The guideline establishes OSFI's expectations related to an FRFI's management of climate-related risk, with three expected outcomes:

1

The FRFI understands and mitigates against potential impacts of climate-related risks to its business model and strategy.

2

The FRFI has appropriate governance and risk management practices to manage identified climate-related risks.

3

The FRFI remains financially resilient through severe, yet plausible, climate risk scenarios and operationally resilient through disruption due to climate-related disasters.

The guidelines also outline OSFI's expectations around an FRFI's governance, strategy and risk management, as well as the disclosure of metrics and targets.

Starting with Internationally Active Insurance Groups (IAIGs) headquartered in Canada, OSFI expects the requirements of B-15 to be fully implemented by 2024.

Not longer than 180 days after the 2024 fiscal year end, IAIGs are expected to have:

- governance structures in place to manage climate risk;
- climate risk incorporated into the strategy;
- climate risk managed in accordance with their risk appetite framework; and
- disclosed climate-related metrics, including Scope 1 and Scope 2 emissions.

2 https://www.osfi-bsif.gc.ca/en/news/osfi-continues-building-climate-resilience

Not longer than 180 days after the 2025 fiscal year end, IAIGs are expected to have:

- disclosed Scope 3 emissions;
- disclosed insurance-associated emissions in relation to property and casualty insurance (excluding mortgage insurance); and
- described the targets used to manage climate risk and their performance against them.

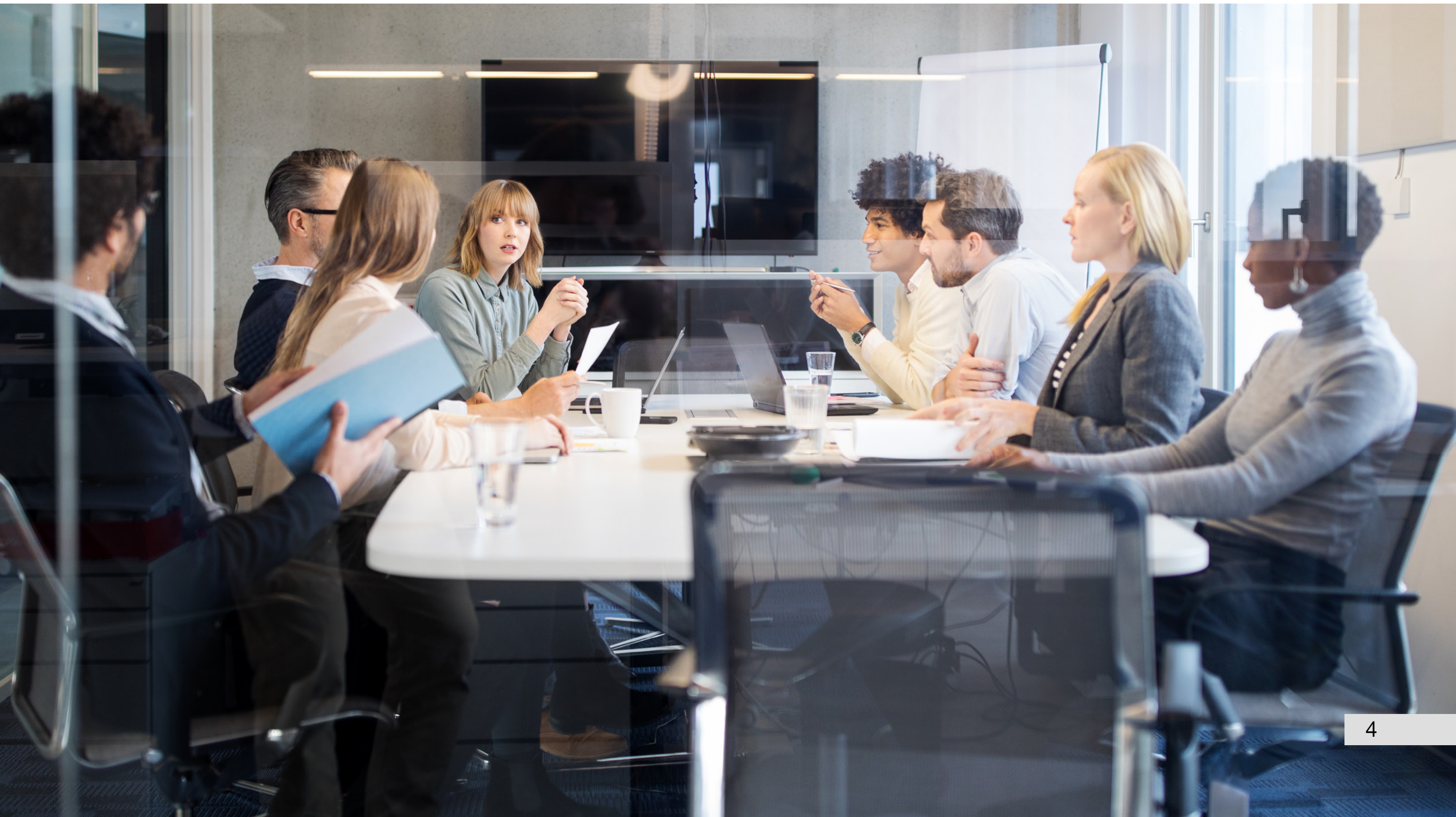
The deadlines for all other federally regulated insurers are extended by one year compared to IAIGs. There are also expectations related to strategy, metrics and targets where the deadline is to be determined.

Standardized climate scenario exercise (SCSE)

The SCSE builds upon OSFI's Guideline B-15 expectations of an FRFI's risk management practices, namely climate scenario analysis. The SCSE applies to IAIGs headquartered in Canada, banks and all other federally regulated insurers.

The focus of the exercise is on understanding an FRFI's potential exposure to climate risks via both transition and physical risks; promoting capacity building for climate risk impact assessments; and providing detailed methodologies and data provisions for accurately mapping and analyzing risks across specific industry sectors.

The expected due date for a completed SCSE is currently December 20, 2024, for all OSFI-regulated insurers.



Other ESG reporting requirements

Given the global reach of Canadian insurance companies, there's the potential that an organization is captured within the scope of multiple ESG reporting jurisdictions. While there's overlap and similarities across the major regulatory bodies in Canada, the United States and the European Union, there are important distinctions worth highlighting below.

EU Corporate Sustainability Reporting Directive (CSRD)

Since the passing of the CSRD legislation in January 2023, there have been 12 initial European sustainability reporting standards (ESRSs) published by the European Financial Reporting Advisory Group (EFRAG). Companies will begin reporting as early as 2025 based on 2024 year-end information.

The ESRSs encompass a wider breadth of sustainability matters than those required to be reported on by OSFI, which are more climate-oriented. Also worth noting is that EFRAG strives to ensure that companies in compliance with the ESRSs are also considered as complying with the ISSB standards to avoid unnecessary multiple reporting.[3]

Canadian companies may fall into the scope of the EU directive as part of any of the following categories:

- The company or its subsidiaries has securities listed on an EU-regulated market (e.g., a dual listing)
- The company has a large EU subsidiary or branch
- The company has a large EU group (e.g., an EU parent of a large group or an EU holding company)

There are also EU insurance companies with Canadian subsidiaries or branches based in Canada that may indirectly have requirements to provide information to support the EU group reporting.

3 https://finance.ec.europa.eu/news/corporate-sustainability-reporting-commission-welcomes-guidance-interoperability-european-and-global-2024-05-02_en

US Securities and Exchange Commission (SEC) climate-related disclosure rules

On March 6, 2024, the SEC adopted final rules designed to enhance public company disclosures related to the risks and impacts of climate-related matters. The new rules include disclosures relating to climate-related risks and risk management as well as the board and management's governance of such risks. On April 4, 2024, the SEC stayed its climate disclosure rules to "facilitate the orderly judicial resolution" of pending legal challenges.[4]

In comparison to the regulations adopted under the CSRD and prescribed by the ISSB, there are some notable exclusions within the SEC's final rules, namely the requirement to disclose Scope 3 emissions. However, there is still a significant number of requirements built into the SEC's final rules regarding the nature and extent of disclosures companies are required to make about the impact of climate-related risks.

Large SEC filers are expected to begin reporting on 2025 information in 2026 for disclosures other than greenhouse gas emissions. The initial compliance dates for other filers and emission-related disclosures are phased in subsequently.

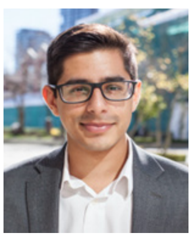
Canadian companies will fall in scope to the SEC's new rules based on SEC registration status.

4 https://www.sec.gov/files/rules/other/2024/33-11280.pdf

A call to action for Canadian insurers

While it appears that reaching a steady state in ESG reporting is at least a few years out, the first set of requirements are already at the proverbial gates. For Canadian insurance companies, the key disclosures are outlined in OSFI's Guideline B-15, but incremental reporting requirements may arise depending on the nature of each company's global footprint and operations. If insurance companies focus on OSFI's Guideline B-15, it will help them build a strong baseline and potentially help them meet the other requirements they may face.

The impetus for companies to build out their ESG reporting capabilities and capacities is clear for all to see. The challenges in navigating the compliance landscape are many, so the timing to get started is today, if not yesterday.



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