



Climate Governance: Equipping Corporate Boards to Mitigate Climate Risks and Seize Climate Opportunities

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Abbreviations

E&S	Environmental and Social
ESG	Environmental, Social, and Governance
GHG	Greenhouse Gas
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
IIA	Institute of Internal Auditors
ISAE	International Standard on Assurance Engagements
ISSB	International Sustainability Standards Board
OECD	Organization for Economic Cooperation and Development
TCFD	Task Force on Climate-Related Financial Disclosures

Climate Governance: Equipping Corporate Boards to Mitigate Climate Risks and Seize Climate Opportunities

Extreme weather events and other effects of climate change can have devastating effects on companies—disrupting value chains, affecting business infrastructure—increasingly presenting unprecedented risks. Often policy reforms and technological changes companies make to address the effects of climate change can upend business models and render once-prized and valuable assets vastly diminished. Yet, with risk can come business opportunities, and both must be appropriately overseen and addressed by corporate boards. Regulators are mandating—and investors are demanding—significant changes in how companies and their boards oversee and manage risks and opportunities associated with climate change, and are clamoring for comprehensive and decision-useful disclosures.

Companies must integrate climate-related risks and opportunities into their business strategy, culture, and values. What specifically does this mean for boards? How can boards both meet the expectations of their stakeholders and build sustainable businesses in the long term? Using its Corporate Governance Methodology (CGM),¹ the International Finance Corporation (IFC) has developed this climate governance guidance and recommended practices to assist boards in identifying and overseeing climate-related risks and opportunities.

Why Climate Governance?

There are five main reasons why climate governance is essential:

1. **Climate change presents risks (and opportunities) that cannot be ignored.** Climate change is recognized as one of the most significant risks companies now face. The Global Risk Reports by the World Economic Forum identify climate-related risks as the top risks. The *Global Risks Report 2023* identifies the four top risks by severity that the world may experience during the next ten years to be: failure to mitigate climate change; failure of climate change adaptation; natural disasters and extreme weather events; and biodiversity loss and ecosystem collapse.²
2. **Climate change drives financial risk and opportunity.** Companies can no longer dismiss climate issues as optional or unimportant for the bottom line. According to the World Economic Forum, “. . . climate change is simply another issue that drives financial risk and opportunity, which boards inherently have the duty to address with the same rigour as any other board topic.”³ The far-reaching effects on company financial performance and board members’ fiduciary duty must be acknowledged and dealt with.
3. **Investor pressure is growing.** The Organization for Economic Cooperation and Development (OECD) found that among forty-two global institutional investors, climate change was the number one issue investors engaged on with companies in 2020, followed by human capital management and board composition and effectiveness.⁴ In addition, large institutional investors, such as BlackRock, have been pressing companies to eliminate greenhouse gas (GHG) emissions by 2050,⁵ and a plethora of investor-led net-zero initiatives have emerged, making it difficult for boards to ignore climate change.
4. **Climate-reporting requirements are increasingly becoming mainstream.** Investors are demanding clear, comprehensive and high-quality information on the material impacts of climate change on the businesses in which they invest. There is a call for companies to enhance and mainstream climate and sustainability disclosure, and to place it on the same footing as financial disclosure. The Task Force on Climate-Related

¹ International Finance Corporation (IFC). IFC Corporate Governance Methodology, October 2018.

https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+cg/investment+services/corporate+governance+methodology.

² World Economic Forum: *Global Risks Report, 2023*. <https://www.weforum.org/reports/global-risks-report-2023/>.

³ World Economic Forum. *How to set up effective climate governance on corporate boards: Guiding principles and questions*. January, 2019. <https://www.weforum.org/whitepapers/how-to-set-up-effective-climate-governance-on-corporate-boards-guiding-principles-and-questions/>.

⁴ OECD. *Climate Change and Corporate Governance*, 2021. <https://www.oecd.org/corporate/climate-change-and-corporate-governance-272d85c3-en.htm>.

⁵ Sorkin, Andrew R., Karaian, Jason, de la Merced, Michael, Hirsch, Lauren, & Livni, Ephrat, 2021. “BlackRock Chief Pushes a Big New Climate Goal for the Corporate World,” *New York Times*, January 26, 2021. <https://www.nytimes.com/2021/01/26/business/dealbook/larry-fink-letter-blackrock-climate.html>.

Financial Disclosures (TCFD)⁶ has created a widely used climate disclosure framework. Additional progress is being made via the International Financial Reporting Standards (IFRS) Foundation, which established the International Sustainability Standards Board (ISSB) in 2021, and published exposure drafts on climate and sustainability disclosure in 2022.⁷ These will form part of a comprehensive global baseline of sustainability disclosure requirements for capital markets.⁸

5. **There is a sharp increase in climate litigation.**⁹ Increasingly, investors and other stakeholders are turning to courts to hold directors and officers accountable for their action or perceived inaction on climate issues in their governance, disclosure, and oversight of risk management and strategy activities. Some plaintiffs claim directors breached their duty of oversight either by failing to implement critical reporting systems or by consciously failing to monitor such systems once in place. Cases target a wider variety of private sector and financial actors, and arguments are increasingly diverse. Examples include claims raising issues around deliberate disinformation (greenwashing cases); failure to disclose and manage climate change risk; damages caused by companies; corporate duty of care in the alignment of major emitters' activities with climate change targets; and cases that challenge specific projects or developments.¹⁰

IFC's Climate Governance Approach

Using its CGM, IFC developed this climate governance approach guidance and recommends practices to assist boards in identifying and overseeing climate-related risks and opportunities. The approach is articulated in a progression matrix to evaluate a company's climate governance practices in each of the six parameters of governance (Commitment to Environmental, Social, and Governance; Structure and Functioning of the Board of Directors; Control Environment; Disclosure and Transparency; Treatment of Minority Shareholders; and Governance of Stakeholder Engagement) along four levels of achievement (from basic to international best practice).

Figure 1. IFC Corporate Governance Methodology Parameters and Climate Governance Focus



Source: IFC

⁶ TCFD is an advisory body set up in 2015 with the support of the G20 and Financial Stability Board (FSB) to address concerns around insufficient financial disclosure of climate-related impacts on business.

⁷ Exposure Draft: IFRS® Sustainability Disclosure Standard. [Draft] IFRS S2 Climate-related Disclosures, March 2022.

<https://www.ifrs.org/content/dam/ifrs/project/climate-related-disclosures/issb-exposure-draft-2022-2-climate-related-disclosures.pdf>.

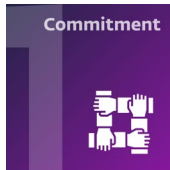
⁸ Additionally, some recent legislative initiatives are requiring climate disclosure, such as the EU Corporate Sustainability Reporting Directive (CSRD), which will require the use of European Sustainability Reporting Standards (ESRS); and the U.S. Securities and Exchange Commission (SEC), which has issued the Enhancement and Standardization of Climate-Related Disclosures. Of note is that the ISSB, ESRS, and the SEC proposal all draw heavily on the disclosure framework introduced by TCFD.

⁹ Climate Governance Initiative and Commonwealth Climate and Law Initiative. *Climate Change Litigation: What board directors need to know*, June 2022.

<https://climate-governance.org/wp-content/uploads/2022/06/CGI-CCLI-Quarterly-Update-1-Climate-Change-Litigation.pdf>.

¹⁰ *Global trends in climate change litigation: 2021 snapshot*, Policy report, July 2021. https://www.lse.ac.uk/granthaminstitute/wp-content/uploads/2021/07/Global-trends-in-climate-change-litigation_2021-snapshot.pdf.

Practices to assist boards in identifying and overseeing climate-related risks and opportunities



Commitment: Create a climate mindset and demonstrate leadership

The tone at the top is a foundational element in creating a corporate culture (ways that people in the organization behave, and the attitudes and beliefs that inform those behaviors) where climate change becomes embedded in corporate strategy and operations. Boards play an active role in building corporate culture and ensuring it is aligned with corporate strategy and objectives. The same holds for corporate commitment to action on climate-related adaptation and mitigation. Commitments should be concrete and, once defined, translated into corporate policies. For example, climate considerations can be woven into existing policies, such as corporate governance codes and codes of ethics, to explicitly include statements related to fiduciary duty, the duty of care, and due diligence as they pertain to climate-related adaptation and mitigation.¹¹

Examples of good practices include: codes of conduct and ethics supporting a shift toward a low carbon supply chain and considering GHG emissions in the product cycle, and appointing an individual as climate lead to evaluate climate-related risks and opportunities as part of the company's internal functions.



Board Structure and Functioning: Active board engagement on climate change

Board engagement on climate issues varies by industry and geography. The guidance below is sector-agnostic and can be adapted to companies' specific circumstances. The key principle, however, is ubiquitous: the board has to require that climate-related risks and opportunities are identified, assessed, and addressed.

Increasingly, there is an expectation that boards are trained on environmental and social (E&S) issues, including climate-related risks and opportunities. As a first step, the board's commitments regarding climate-related issues must be clearly established (as noted in the previous section), and training must be provided to achieve an adequate level of literacy so that directors can recognize climate issues relevant to the company and can understand their duty with respect to these issues.

Good international practices related to a board's role in oversight of climate-related adaptation and mitigation include the following:

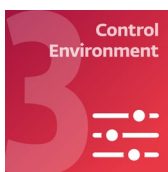
- The board includes climate-related risks and opportunities as recurring agenda items, including measures to reduce GHG emissions and to increase resilience; and the board approves climate-related strategy, policies, and targets.
- The board receives regular training on sector-specific climate-related risks and opportunities.
- The board requires that the company strategy, the business model, and financial planning (short-, medium-, and long term) consider environmental, social, and governance (ESG) (including climate-related risks and opportunities).
- At least one director has experience analyzing and interpreting climate-related risks and opportunities.
- In industries with heightened exposure to climate risks, at least one director is climate-literate, with knowledge or experience in managing climate-related risks, impacts, and opportunities.

¹¹ Climate Disclosure Standards Board (CDSB). *Statement on Fiduciary Duty and Climate Change Disclosure*. https://www.cdsb.net/sites/default/files/statement_on_fiduciary_duty_and_climate_change_disclosure.pdf.

- The board (via the remuneration committee) adopts climate-related targets for executives (including not allowing growth and economic performance at the cost of adverse climate impacts) and incorporates climate-related awareness skills and experience in board succession planning.
- The board and management evaluation includes consideration of climate-related risks and opportunities.

Examples of leading oversight practices also include monitoring and oversight of progress toward goals and science-based targets for decarbonization, including climate-related adaptation and mitigation¹² and ensuring that the company has set an internal price on carbon to understand how climate change affects the company. Additionally, in more advanced companies, board and executive incentives need to be aligned to promote the purpose, strategy, and long-term prosperity of the company, and should include climate-related targets and indicators in the remuneration policies and executive incentive schemes to achieve net zero.

Some companies with higher exposure to climate change have established a separate board committee responsible for oversight of climate-related risks and opportunities. For others, it may be sufficient to augment the duties of existing committees (such as audit, risk, or sustainability) with such responsibilities.



Control Environment: Integrate climate-change issues into key systems and functions

Internal Control System

Climate-related risks and opportunities should be incorporated into internal control policies and procedures; and staff should be adequately trained on industry climate-related risk issues. Requiring contractors, subcontractors, third parties, suppliers, supply chain workers, and the value chain to adhere to these established policies and procedures is also considered good international practice. For example, the procurement policy should be revised so that E&S and climate-related risks and opportunities across the company’s operations and value chain are captured adequately. Ideally, structures and activities would be patterned after the Three Lines Model by the Institute of Internal Auditors (IIA).¹³ The audit committee plays a key role in overseeing the implementation of corrective action for any control deficiencies identified in internal audit reports.

Internal Audit Function

The internal audit function should include: incorporating climate change into the work plan; conducting periodic audits of climate-related data collection, risk register, policies, procedures, and controls; reviewing the verifiability and accuracy of climate-related data, as well as the comprehensiveness of data required by the regulators, and reporting the results to the audit committee.

Leadership-level practice includes the internal audit functions of:

- Providing quality assurance, aligned with enforceable and leading disclosure standards, for climate-related data and information reported
- Routinely auditing climate-related aspects of governance, strategy, risk management, metrics, and targets
- Communicating regularly with the board and management on the internal audit’s activities related to physical and transitional risks

¹² IFRS Sustainability Disclosure Standards (IFRS S1 General Sustainability-related Disclosures and IFRS S2 Climate-related Disclosures), and *Task Force on Climate-related Financial Disclosures*, 2022 Status Report. Hereinafter “TCFD Implementation Strategy.” <https://assets.bbhub.io/company/sites/60/2022/10/2022-TCFD-Status-Report.pdf>.

¹³ IIA. *The IIA’s Three Lines Model: An update of the Three Lines of Defense*. <https://www.theiia.org/globalassets/documents/resources/the-iias-three-lines-model-an-update-of-the-three-lines-of-defense-july-2020/three-lines-model-updated-english.pdf>.

- Addressing the distinct challenges of auditing climate-related opportunities and forward-looking statements and commitments in the public domain in all aspects of the function (planning, audits, communications, etc.)

Risk Governance

Risk governance is a key board responsibility, including climate-risk governance. A key component of this obligation is ensuring that climate-related risks are integrated into the overall risk-management framework of the organization and that adequate adaptation measures are implemented.¹⁴ Management should provide the board with the full assessment of climate-related risks and opportunities related to the company's products, services, emissions, and physical footprint, as well as their potential impact on the financial position and current strategy.¹⁵ Based on this information, the board should oversee the implementation of adequate mitigation and adaptation measures. Additionally, the board (or risk management committee or other specialized committees) should check that management conducts annual scenario analyses to evaluate the company's resilience, including a 1.5–2°C scenario or lower.

Compliance Function

The compliance function plays a key role in climate risk mitigation as well. The board should encourage the establishment of an adequate compliance function and should periodically review its adequacy. Mechanisms need to be in place to identify and report wrongdoing and misconduct related to climate-related compliance lapses—including, but not limited to, noncompliance with climate provisions in climate policies and procedures and the code of ethics or conduct. Best practices would additionally require that the compliance program applies to contractors, subcontractors, and suppliers.



Disclosure and Transparency: Share climate data with stakeholders

IFC has been promoting a flexible approach to corporate disclosure and transparency, which enables companies to address aspects of specific relevance to their market and stakeholders. Detailed advice on disclosure is available in IFC's *Beyond the Balance Sheet: IFC Toolkit for Disclosure and Transparency*.¹⁶ As with other elements of IFC's CGM, disclosure practices are presented as a progression, starting from basic practices up to the leadership level, as required, as illustrated in Figure 2 below.

¹⁴ World Economic Forum. *Climate Governance*, 2019, Principle 5.

https://www3.weforum.org/docs/WEF_Creating_effective_climate_governance_on_corporate_boards.pdf.

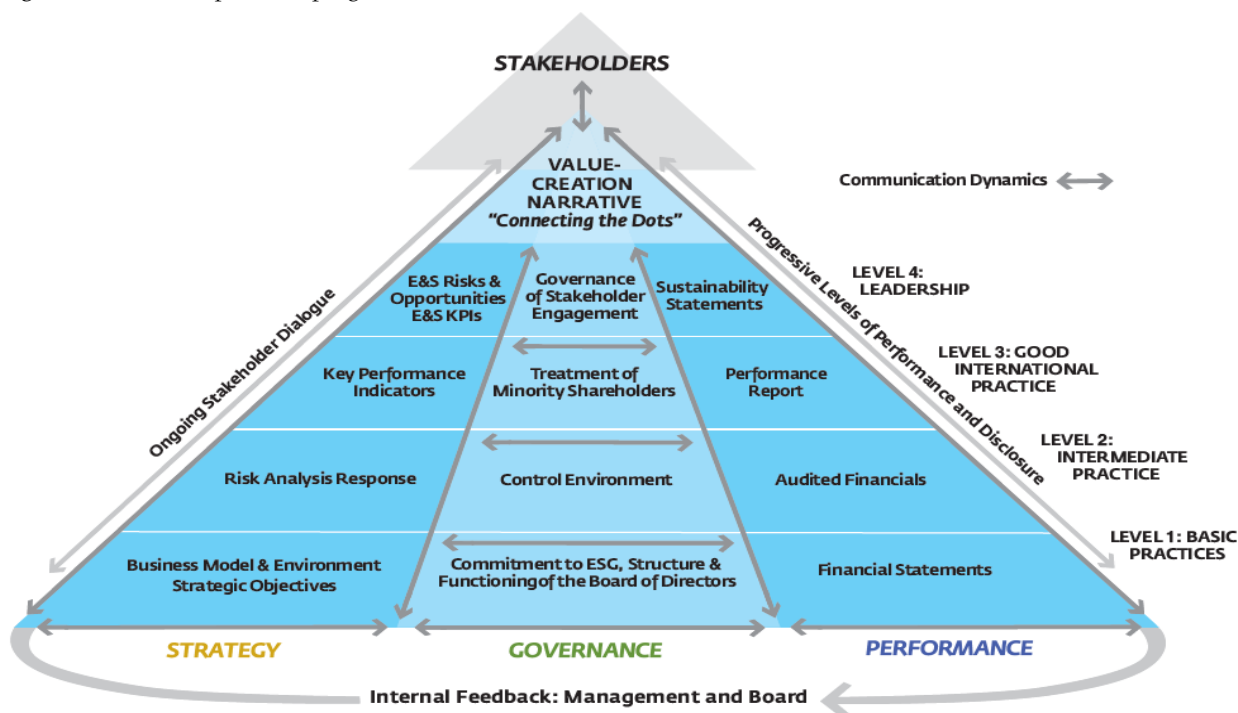
¹⁵ Chartered Institute of Internal Auditors. The Climate Group. *Organisations' preparedness for climate change: An internal audit perspective*, 2021.

<https://www.iaa.org.uk/media/1691707/organisations-preparedness-for-climate-change-final-report.pdf>.

¹⁶ International Finance Corporation (IFC). *Beyond the Balance Sheet: IFC Toolkit for Disclosure and Transparency*, 2018.

https://www.ifc.org/wps/wcm/connect/d4bd76ad-ca04-4583-a54f-371b1a7e5cd0/Beyond_The_Balance_Sheet_IFC_Toolkit_for_Disclosure_Transparency.pdf?MOD=AJPERES&CVID=morp0vo.

Figure 2. Disclosure practices progression



Note: The progressive levels of performance and disclosure are cumulative, whereby each level also integrates practices of the preceding levels.
Source: IFC.

Source: IFC, Beyond the Balance Sheet Toolkit for Disclosure and Transparency

Regarding climate reporting specifically, multiple reporting standards are accessible with some valuable convergence as of late. TCFD's approach in integrating climate disclosures into annual financial filings is one of the most widely accepted approaches and conveys the direct link between climate risk and opportunity treatment and financial performance.

At the most basic level, climate-related disclosures are established by local jurisdictional requirements. If a jurisdiction has no applicable climate-related requirements, then climate-related risks, opportunities, and linked impacts should be disclosed in a separate sustainability or TCFD report. To further assure stakeholders of the reliability and verifiability of data, all climate governance, strategy, and climate-related risk management activities should be disclosed, together with GHG¹⁷ Scope 1 and Scope 2 emissions (on an intensity and absolute basis), and the methodology used to calculate GHG emissions and Scope 3 emissions.

More advanced climate disclosure practices include:

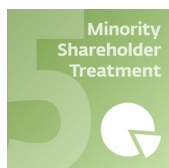
- Disclosing commitment to achieving net zero by 2050 or earlier
- Reporting on the targets set for addressing climate-related risks and opportunities, the objective and period they apply to, and progress toward achieving the targets and net zero interim targets¹⁸
- Disclosing scenario analysis and cross-industry climate-related metrics, including how scenarios were identified as appropriate for selection and application¹⁹

¹⁷ TCFD Implementation Strategy.

¹⁸ Ibid.

¹⁹ Ibid.

- Obtaining negative or limited assurance on sustainability reporting and climate-related disclosures
- Subjecting ESG and climate-related data to annual reasonable assurance attestation by an independent provider under International Auditing and Assurance Standards Board (IAASB) Standards,²⁰ International Standard on Assurance Engagements (ISAE) reports ISAE 3000 or ISAE 3410²¹
- Disclosing climate-related risks, opportunities, and impacts on the company and the company's impact on the climate (double materiality including financial and impact materiality)



Minority Shareholder Treatment: Include shareholders in climate-related decision-making

Shareholders are increasingly requesting involvement and information on how companies deal with climate issues. As noted above, disclosure practices are key for shareholders to understand how the company's business is impacted by (and impacts) the climate. Some companies follow good international practices of consulting shareholders on climate-related transition action plans. Such plans can also be approved by shareholders and include a commitment to net zero by 2050 or earlier. Some shareholders are also calling for climate targets to be included in remuneration plans. Shareholder activism on climate is expected to increase.



Governance of Stakeholder Engagement: Involve those impacted

Stakeholders play a major role in the climate agenda. To effectively oversee climate-related risks and opportunities, companies must consider stakeholder interests. Regulators and non-governmental organizations are monitoring companies' commitment to climate action and working to detect and prevent greenwashing.

As a starting point, companies should conduct stakeholder identification and mapping—including climate-related impacts on contracted workers, primary supply chain workers, and neighboring communities—with a diversity, equity, and inclusion (DEI) lens. The senior executive responsible for stakeholder relationships should see that climate-related risks and opportunities are integrated within strategies and target setting. And, most importantly, the board should maintain regular exchanges and dialogue with stakeholders—such as peers, policymakers, regulators, civil society organizations, and investors—to encourage the sharing of GHG emissions-assessment methodologies and to stay informed about the latest climate-relevant risks and opportunities as well as regulatory requirements and standards.²²

Example of Climate Governance Disclosure: Nedbank, South Africa

Nedbank Group Limited, headquartered in Sandton, South Africa, has adopted a good, structured approach to climate governance and has been able to fully disclose its climate-governance approach, as demonstrated in its 2021 *TCFD Report*.²³ The company reports on integrating climate risks into its overall Enterprise Risk Management (ERM) Framework. Additionally, its climate-governance approach is incorporated into board practices, operations of business lines (from lending, investing, and asset management to a bank's own operations), and direction setting. The report discloses the scope and meeting frequency of relevant committees, as well as cross-committee collaboration to achieve a

²⁰ International Standards on Auditing (ISA) most relevant to climate change risks: 200, 250, 260, 315, 320, 330, 450, 540, 570, 620, 700, 701, 705, 720.

²¹ International Auditing and Assurance Standards Board™ (IAASB), International Standard on Assurance Engagements (ISAE). *ISAE 3000 (Revised), Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, 2013.

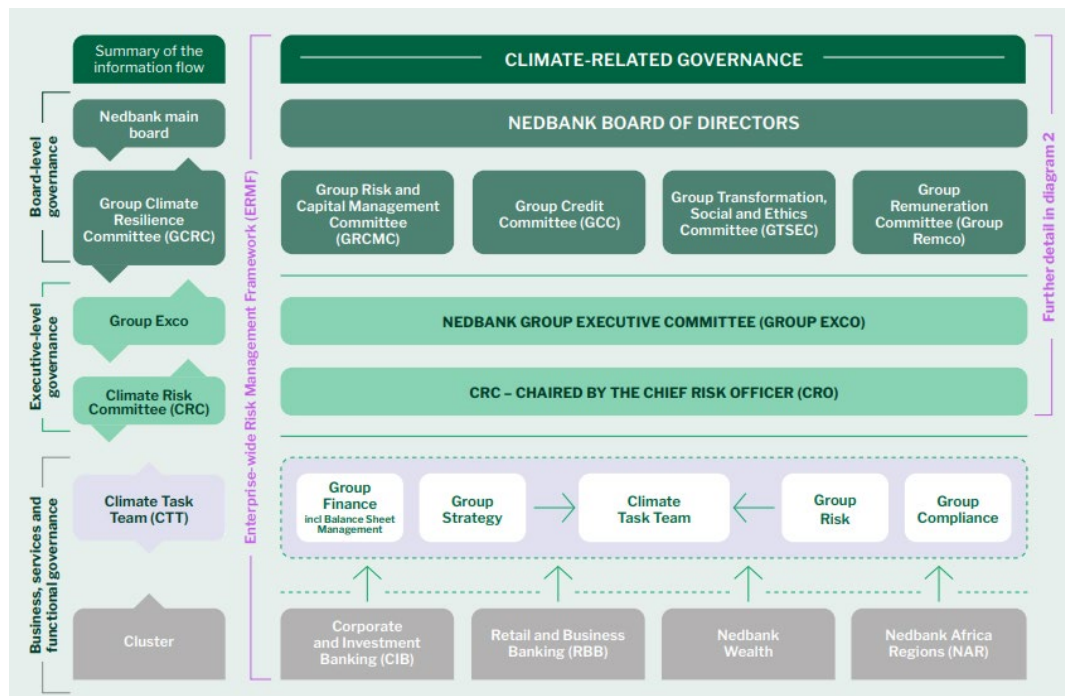
<https://www.ifac.org/system/files/publications/files/ISAE%203000%20Revised%20-%20for%20IAASB.pdf>; ISAE 3410, *Assurance Engagements on Greenhouse Gas Statements*, 2013. https://www.ifac.org/system/files/publications/files/Basis%20for%20Conclusions%20-%20ISAE%203410%20Assurance%20Engagements%20on%20Greenhouse%20Gas%20Statements-final_0.pdf.

²² World Economic Forum, 2019, Principle 8. https://www3.weforum.org/docs/WEF_Creating_effective_climate_governance_on_corporate_boards.pdf. Note that if the company is a financial institution, it should communicate its climate finance practices to external stakeholders.

²³ Nedbank Group. *Task Force on Climate-related Financial Disclosures (TCFD) Report*, 2021. [https://www.nedbank.co.za/content/dam/nedbank/site-assets/AboutUs/Information%20Hub/Integrated%20Report/2022/2021%20Nedbank%20Group%20TCFD%20Report%20\(AA\).pdf](https://www.nedbank.co.za/content/dam/nedbank/site-assets/AboutUs/Information%20Hub/Integrated%20Report/2022/2021%20Nedbank%20Group%20TCFD%20Report%20(AA).pdf).

holistic approach to manage climate risks and opportunities. The report also includes information on management responsibility, staff training, and awareness raising on climate issues.

Figure 3. Climate-related governance at Nedbank



Source: Nedbank, 2021 TCFD Report, 2022

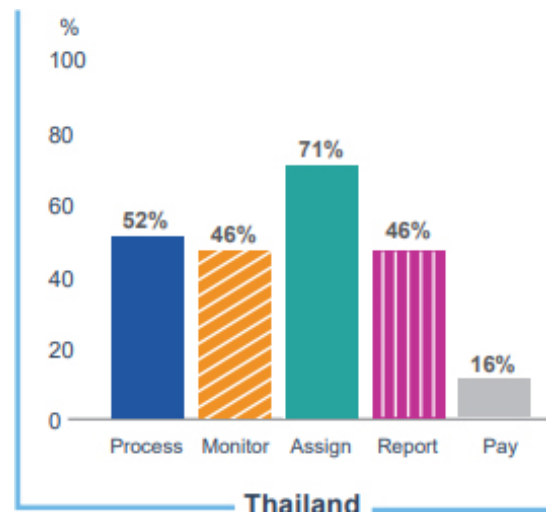
Example: Improving Climate Governance Practices in Thailand

In 2022, the Global Reporting Initiative (GRI) conducted a study on climate-disclosure practices by the top 100 companies by market capitalization across six Association of Southeast Asian Nations (ASEAN) economies.²⁴ They analyzed sustainability reports to determine the existence of reporting on five topics: processes that boards and their committees use to keep themselves informed of climate-related issues; how boards monitor progress against climate goals and targets; assigned climate responsibilities at the management level; management reporting to the board or its committees on climate; and the existence of remuneration policies for the board and management which account for climate risks.

As illustrated in Figure 4, showing results for climate disclosures in Thailand, it is encouraging to see the high level of disclosure on assigned climate responsibilities at the management level (71% of surveyed companies from Thailand report having clearly assigned responsibilities on climate to management). More work needs to be done, however, on explaining which processes are in place to keep the board and its committees informed of climate-related risks (52% of companies reported having such processes), as well as adequate monitoring and reporting (46% of companies reported having those in place), all of which are prerequisites for creating a comprehensive climate governance framework. It is also evident that the link to remuneration is only an emerging issue, with only 16% of companies reporting that remuneration policies for the board and management incorporated climate risks.

²⁴ Global Reporting Initiative (GRI), Centre for Governance and Sustainability, NUS Business School. *Climate reporting in ASEAN: State of corporate practices*, July 2022. <https://www.globalreporting.org/media/oujbt3ed/climate-reporting-in-asean-state-of-corporate-practices-2022.pdf>.

Figure 4. Climate disclosures in Thailand

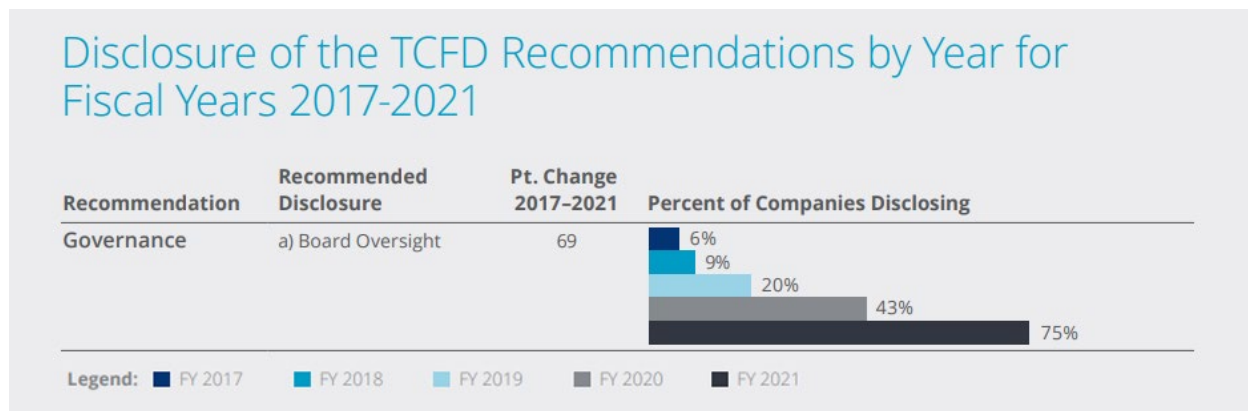


Source: Global Reporting Initiative (GRI). Climate Reporting in ASEAN: State of Corporate Practices, July 2022

Example: Positive Trends in Climate Reporting

TCFD’s 2022 Status Report²⁵ shows significant progress in implementing recommended disclosures and an overall increase in the disclosure of climate-related information since 2019. In a survey conducted in 2022 with asset owners, asset managers, and companies from five regions, TCFD looked at disclosures related to governance, strategy, risk management, and metrics and targets. Related to governance specifically, the report found that in 2022, 75 percent of companies disclosed information on board oversight of climate-related issues—an increase from six percent in 2017.

Figure 5. Disclosure of the TCFD Recommendations by Year for Fiscal Years 2017–2021



Source: Task Force on Climate-related Financial Disclosures, 2022 Status Report.

²⁵ Task Force on Climate-Related Financial Disclosures (TCFD). *Task Force on Climate-related Financial Disclosures: 2022 TCFD Status Report*. <https://assets.bbhub.io/company/sites/60/2022/10/2022-TCFD-Status-Report.pdf>.



Conclusion

The tone at the top is the foundational element of effective corporate climate action. Of paramount importance are a board's identification, assessment, and action on climate-related risks and opportunities. These functions are achieved by incorporating climate into strategy deliberations and creating systems to identify, monitor, and respond to climate-related issues. As expectations of investors and other stakeholders grow regarding how companies address climate-related issues, it is crucial to establish and maintain robust disclosure practices and to collect and disseminate reliable data to assure the credibility of a company's long-term prospects. Lastly, boards must help determine a just and equitable transition; and consider how their decisions on business model changes impact the employees, the supply chains, and the communities in which they operate. Boards are uniquely positioned to combine climate change action with corporate purpose and strategy and thus are uniquely positioned to lead the fight against climate change.

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