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The new frontier of nature-related financial disclosures: what the finance industry needs to know

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On Jan. 16, 2024, at this year's annual World Economic Forum meeting in Davos, Switzerland, it was announced that 320 organizations from more than 46 countries have committed to start making nature-related disclosures based on the recommendations of the Taskforce on Nature-related Financial Disclosures (TNFD) for nature-related risk and opportunity management and disclosure (the Recommendations), which were published in September 2023 accompanied by a set of implementation guidance. The TNFD initiative was led by a taskforce of 40 members, representing more than US $20 trillion in assets under management, with global market input and participation.

This first cohort of adopters of the Recommendations includes leading publicly listed companies across geographies and industry sectors representing US $4 trillion in market capitalization; more than 100 financial institutions, including some of the world's largest asset owners and managers, representing US $14 trillion in assets under management; as well as banks, insurers, and other leading market intermediaries such as stock exchanges and audit and accounting firms, each signaling their intention to begin adopting the Recommendations and publishing TNFD-aligned disclosures as part of their annual corporate reporting for FY2023, FY2024, or FY2025.

The TNFD's Recommendations and guidance provide a practical basis for organizations to get started on identifying, assessing and disclosing their nature-related dependencies, impacts, risks and opportunities, increasing the scope and ambition of their disclosures over time. The recommended disclosures are a combination of qualitative process-oriented disclosures and others requiring data and analytics. Like its climate counterpart, the Taskforce on Climate Related Disclosures (TCFD) is a voluntary framework which governments and regulators can, if they choose, make mandatory locally or leave as voluntary, or standard setters can rely on in their own work.

The TNFD's Recommendations are a key milestone in the relationship between nature, business, and financial capital, positioning nature risk alongside financial, operational, and climate risk and integrating nature into strategic and capital allocation decision-making, helping to shift capital flows to nature-positive outcomes.

The Recommendations also align with the goals of the Kunming-Montreal Global Biodiversity Framework (the GBF), which was adopted by 196 countries at the 2022 United Nations Biodiversity Conference of Parties (COP15), to halt and reverse nature loss. The TNFD guidance will help the market participants get started with nature-related integrated assessment and corporate reporting. Before taking a closer look at this development, we should consider the context.

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Biodiversity loss and ecosystem collapse rank fourth in the World Economic Forum's 2023 top 10 global risks, behind failure to mitigate and adapt to climate change (ranked first and second, respectively) and natural disasters and extreme weather events (ranked third). In his review of biodiversity economics for the UK government, the eminent Professor Sir Partha Dasgupta supported the view that nature is an asset, just as produced capital (roads, buildings, and factories) and human capital (health, knowledge, and skills) are assets, "The Economics of Biodiversity: The Dasgupta Review," February 2021.

However, nature is at a distinct disadvantage to other assets because much of nature is open to everyone at no monetary charge; as a result, market prices do not reflect its worth to society. The vital ecosystem services on which businesses and society depend are not being appropriately priced by businesses and financial markets. Without a transformative change, demands on nature will continue to exceed what nature can supply on a sustainable basis.

The degradation of nature and actions aimed at conserving, restoring, and sustainably using it present significant risks and opportunities for businesses, finance, and society. Central banks and financial supervisors are increasingly recognizing nature loss as a source of systemic risk to financial systems and economies.

Governments are mobilizing too. At COP15 in December 2022, almost 200 governments committed to ambitious goals and targets under the GBF to halt and reverse nature loss by 2030, and by 2050 see a world where nature is valued, conserved, restored, and wisely used. Target 15 of the GBF calls on governments to take legal, administrative, or policy measures to encourage and enable businesses to monitor, assess, and disclose their risks, dependencies, and impacts on biodiversity.

To achieve these goals, companies, lenders, and investors must first understand their own nature-related dependencies, impacts, risks, and opportunities to account adequately for nature in their strategies and capital allocations. Many policymakers, regulators, asset owners, asset managers, and leading global companies are now focusing more on nature-related risk management and mobilizing the private sector to tackle nature loss and scale-up nature-based solutions.

The Recommendations, which are consistent with and designed to enable the achievement of the goals and targets of the GBF, are based on the same four pillars as the TCFD, which was launched in 2015 and has seen remarkable global take-up, both mandatory and voluntary: governance of nature-related dependencies, impacts, risks and opportunities, strategy (including nature-related issues that the organization has identified over the short, medium, and long term, as well as their effect on the business model, value chain, and financial or transitional planning and strategy), risk and impact management (including processes for identifying and managing nature-related issues in direct operations and upstream and downstream value chains), and metrics and targets used to assess and manage nature-related dependencies, impacts, risks, and opportunities.

Each pillar is accompanied by a set of recommended disclosures, numbering 14 in total. They are designed to allow organizations to get started now and increase their disclosure ambition over time in partial recognition of significant gaps in the availability of relevant data.

The Recommendations have also been designed to be consistent with the new S1 and S2 standards on sustainability reporting published in mid-2023 by the International Sustainability Standards Board (ISSB) as well as nature and biodiversity impact reporting standards provided to market participants by the Global Reporting Initiative (GRI).

On Jan. 25, 2024, GRI, a significant sustainability standard-setter, proposed updates to its standard for how companies should report biodiversity impacts throughout their operations and value chains that will go into effect for GRI-reporting companies in 2026. The standards are, in GRI's words, "to a high extent consistent" with the Recommendations. Notably, while ISSB takes a single materiality approach, GRI takes a double-materiality approach.

The final version of the Recommendations featured three main differences from the previous beta versions, being disclosures:

- to describe the organization's human rights policies and engagement activities and oversight by the board regarding affected indigenous peoples, local communities, and affected stakeholders;
- of locations of assets and/or activities in the organization's direct operations and its upstream and downstream value chains; and
- of the organization's nature-related dependencies, impacts, risks, and opportunities in its upstream and downstream value chains. Notably, TNFD recognizes the challenges associated with reporting across the value chain relating to the provision of data.

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Plastic pollution has now been introduced as a core global impact and dependency indicator. Disclosure of Scopes 1, 2, and 3 GHG emissions under the metrics and targets heading has been dropped in favor of metrics used by the organization to assess and manage dependencies and impacts on nature.

On the challenging issue of materiality, the Recommendations accommodate both financial materiality and impact materiality depending on the jurisdictional requirements applicable to the organization, using the ISSB corporate sustainability disclosure standards for financial materiality and the approach of the GRI for impact materiality.

Alongside the Recommendations, TNFD has produced an accessible (and optional) internal due diligence assessment process explaining how project teams within organizations can practically identify, assess, manage, and disclose nature-related issues, known as "LEAP" (Locate, Evaluate, Assess, and Prepare).

Asset managers, for example, will likely need to source and collect new information about their own material nature-related issues to be able to adopt the Recommendations, engaging closely with their portfolio companies. The LEAP approach provides a practical guide on how these issues can be scanned and triaged, even with limited internal data and knowledge.

TNFD has published specific guidance for financial institutions that is intended for banks, insurers, asset managers, and owners, recognizing that their nature-related impacts and dependencies are primarily generated through their investment portfolios rather than their direct operations, rendering them dependent on their investors, portfolio companies, customers, and clients, and reliant on external data providers, proxy, and/or modeled data.

Financial institutions will face the challenge of data gaps as the availability and quality of nature-related data continue to evolve. That said, the majority of the Recommendations cover process descriptions that do not require quantitative metrics. Where quantitative data is required but not available, consideration should be given to the use of secondary, modeled, and/or proxy data and estimates. TNFD recognizes that disclosure ambition will increase over time and does not want perfection to stand in the way of early adopters.

While the cause of climate change reduction and regulatory adoption of TCFD was turbo-charged by the Paris Agreement on Climate Change (with its net-zero targets), we can expect regulatory adoption of the Recommendations around the world relatively quickly, propelled by the 2030/2050 ambition of the GBF and the scale of early take-up by the market. Corporates, financial institutions, asset managers, and owners that seek to comply with the Recommendations should consider preparing now for nature-related sustainability reporting to sit alongside increasingly mainstream climate-related sustainability reporting.

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