Canada Climate Law Initiative | L'Initiative canadienne de droit climatique

From:
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To:
The Honourable Danielle Smith
Premier, Government of Alberta
premier@gov.ab.ca

and to:
The Honourable Nate Horner
Minister of Finance
and President of Treasury Board
Government of Alberta
tbf.minister@gov.ab.ca

Dear Premier Smith and Minister Horner,

Re: Policy Submission to Alberta Government on Strengthening Climate Resilience in the Financial Services Sector

Policies to help Albertans become financially resilient to the impacts of climate change are critically important. Alberta experienced more than 1,000 wildfires in 2023, with 48 communities affected and more than 38,000 Albertans evacuated.[1] It was unprecedented in terms of area burned, severely impacting air quality, human health, First Nations communities, wildlife, ecology, and agriculture, with significant knock-on economic impacts. Flood hazards and atmospheric rivers are also increasing in frequency and have devastated many areas of Alberta.[2] The Alberta government has stated its support of a net-zero emissions power grid[3] and carbon-neutral oil and gas sector by 2050.[4] You now have a unique opportunity to offer leadership in advancing policy that will attract new capital to support the transition.

The Canada Climate Law Initiative (CCLI) submits that three key policy recommendations have the potential to considerably enhance the Alberta government's oversight of financial services. Alberta is a key

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[1] Government of Alberta, "Alberta Wildfire Status Dashboard, January 1 - December 31", Alberta Wildfire Status Dashboard (arcgis.com); Government of Alberta, "Alberta's 2023 wildfire season was the province's busiest on record, with the largest area ever burned" (3 November 2023), Alberta's wildfire season has come to an end | alberta.ca.
[2] Government of Alberta, "Overview", Flood preparedness | Alberta.ca.
[3] "Alberta premier tells climate conference renewable-powered grid by 2035 'fantasy thinking'", CBC News, (26 October 2023), Alberta premier tells climate conference renewable-powered grid by 2035 'fantasy thinking' | CBC News.
[4] Minister Rebecca Schulz, "A practical path forward", (19 July 2023), A practical path forward: Minister Schulz | alberta.ca.

part of the Canadian economy, with 13 credit unions in Alberta with total assets of $30.9 billion and total deposits of $26.4 billion;[5] 228 insurance entities licensed in the province;[6] and 653 Alberta-regulated pension funds with $57.4 billion in assets under management.[7] Given the importance of these financial institutions to both the provincial and national economies, the Alberta government has the potential to be a leading presence in encouraging investment in projects, activities, and sectors that will support the transition to a net-zero carbon economy. These recommendations, if implemented, will strengthen regulatory oversight and contribute to long-term economic competitiveness in the province, while showcasing a commitment to proactive climate action in support of industry actions already underway such as the Pathways to Net Zero Alliance created by Canada's largest oil sands producers.

The CCLI is a collaboration of the law faculties at the University of British Columbia and York University that analyses the legal obligations of corporate directors, pension fiduciaries, and asset managers to manage and report on climate-related financial risks and opportunities. It publishes guidance on effective climate governance, working closely with legal and accounting professionals and policymakers.[8] CCLI believes our three recommendations would effectively amplify Alberta's protection of the safety and soundness of the financial system by offering guidance to Alberta-regulated financial institutions on managing climate-related financial risks and building resilience in the transition to a decarbonized economy.

Our recommendations:

1. Adopt a guideline on climate financial risk management for Alberta-regulated financial institutions aligned with the federal Office of the Superintendent of Financial Services (OSFI) Guideline B-15 Climate Risk Management.

2. Endorse the Sustainable Finance Action Council's proposed Green and Transition Finance Roadmap and co-operate as a member of the proposed Taxonomy Council's Indigenous, Provincial and Territorial Government Stakeholder Advisory Group in advising the Taxonomy Council.

3. Amend the Alberta Employment Pension Plans Regulation 154/2014 to require that the pension plan administrator's written statement of investment policies and procedures (SIPP) includes a statement on how its policies and procedures address climate-related financial risks, including the plan's climate resilience (mitigation and adaptation) and how it weighs the risks and benefits in decisions with respect to its portfolio of investments and loans in light of the impending transition to a net-zero emissions economy.

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[5] As of August 2023, List of Credit Unions registered in Alberta - August 14, 2023. See also Credit Union Deposit Guarantee Corporation, Annual Report 2022, CUDGC Annual Report 2022.pdf at 4, 12.
[6] As of December 31, 2022, Superintendent of Insurance 2022 Annual Report, at 5, Superintendent of Insurance 2022 Annual Report (alberta.ca).
[7] As of December 31, 2017, the latest information available on the government's website as of November 2023, the Superintendent's Office was responsible for the supervision of 723 pension plans; 653 of which had registered status under AEPPA, covering 280,750 members were supervised by the Superintendent's Office; 2017 Pensions Annual Statistics Report - released August 20, 2018 (alberta.ca).
[8] See for example, in financial services, Janis Sarra and Norie Campbell, *Banking on a Net-Zero Future: Effective Climate Governance for Canadian Banks* (CCLI 2022); Janis Sarra, *Life, Health, Property, Casualty: Canadian Insurance Company Directors and Effective Climate Governance* (CCLI 2021); Janis Sarra, Roopa Davé, Meghan Harris-Ngae, and Ravipal Bains, *Audit Committees and Effective Climate Governance, A Guide for Boards of Directors* (CCLI, 2020) (all in both French and English).

Recommendation 1: Adopt a guideline on climate financial risk management for Alberta-regulated financial institutions aligned with the federal Office of the Superintendent of Financial Services (OSFI) Guideline B-15 Climate Risk Management.

Alberta has an opportunity to demonstrate leadership by issuing guidance on climate-related financial risk management. The Alberta Superintendent of Financial Institutions (AFSI), as part of its oversight of Alberta-regulated financial institutions, is responsible for minimizing the risk of loss to deposit holders and consumers of trust products in Alberta; promoting a level, fair, and competitive environment for financial institutions in Alberta; and overseeing the deposit-taking institutions marketplace in Alberta, including the regulation of financial institutions operating in Alberta.[9] Adoption of a guideline on climate financial risk management aligned with the OSFI Guideline B-15 Climate Risk Management[10] would considerably enhance these oversight functions that are critically important to the soundness of Alberta's financial system. With the new transfer of regulatory oversight responsibility for credit unions from Alberta Central to the Credit Union Deposit Guarantee Corporation (CUDGC) effective 31 January 2023, there is an opportunity for more effective oversight of the entire credit union system.[11] CUDGC's express goal is to be proactive and preventive in its supervisory approach in monitoring and regulating Alberta credit unions to maintain adequate capital and enable a safe and sound credit union system.[12]

The CCLI submits that Alberta's adoption of a guideline on climate risk management would recognize that building resilience against climate-related risks requires financial institutions to address vulnerabilities in their business model, their overall operations, and their balance sheet using forward-looking approaches that are holistic, integrated, and built on reliable empirical data and sound analyses.[13] It does not preclude investments in energy-intensive trade exposed sectors, but informs investments and unlocks investment through an informed and evidence-based lens with the understanding that transition investments in projects are critical and globally relevant to a net-zero Paris Agreement-aligned future. Guideline B-15 recognizes that climate risks and vulnerabilities will vary with a financial institution's size, nature, scope, complexity of its operations, and risk profile.[14] We submit that Alberta should adopt the five principles in Guideline B-15 to align the safety and soundness of the Alberta financial services sector. Specifically, the Alberta guideline should adopt:

> Principle 1: The financial institution should have the appropriate governance and accountability structure in place to manage climate-related risks; should disclose the board of directors' oversight of climate-related risks and opportunities and management's responsibility for assessing and managing climate-related risks and opportunities; and consider whether senior management compensation policies and practices should incorporate climate-related risk considerations.
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> Principle 2: The financial institution should implement a "climate transition plan" in line with incorporating climate risk management in its business plan and strategy to guide its actions to manage increasing physical risks from climate change and the risks associated with its transition towards a low-

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[9] Financial institutions – Overview | Alberta.ca. Pursuant the *Insurance Act,* the Superintendent of Insurance may issue guidelines to clarify expectations with respect to interpretation and application of the *Insurance Act* and its regulations; Superintendent of Insurance 2022 Annual Report Superintendent of Insurance 2022 Annual Report (alberta.ca).
[10] Office of the Superintendent of Financial Services (OSFI), OSFI Guideline B-15 Climate Risk Management, (March 2023) Guideline B-15 - Climate Risk Management (osfi-bsif.gc.ca).
[11] Credit Union Deposit Guarantee Corporation, Annual Report 2022, note 5 at 4.
[12] Alberta *Credit Union Act,* Revised Statutes of Alberta 2000 Chapter C-32, as amended; and CREDIT UNION DEPOSIT GUARANTEE CORPORATION (cudgc.ab.ca); see also CUDGC Annual Report 2022.pdf at 18.
[13] Guideline B-15, note 10 at 1.
[14] Guideline B-15, note 10 at 2.

greenhouse gas (GHG) economy, assessing achievability of its plan under different climate-related scenarios and measuring progress through internal metrics and targets.

Principle 3: The financial institution should manage and mitigate climate-related risks in accordance with its Risk Appetite Framework and Enterprise Risk Management (ERM) framework, monitoring and reporting relevant internal metrics, limits, and indicators to assess the effectiveness of its climate risk management.

Principle 4: The financial institution should use climate scenario analysis to assess the impact of climate-related risks on its risk profile, business strategy, and business model.

Principle 5: The financial institution should maintain sufficient capital and liquidity buffers for its climate-related risks, incorporating climate-related risks into its Internal Capital Adequacy Assessment Process (ICAAP) or Own Risk and Solvency Assessment (ORSA) process.[15]

The CCLI submits that Alberta should adopt OSFI's three expected outcomes, specifically, that Alberta financial institutions understand and mitigate against potential impacts of climate-related risks to their business model and strategy; should have appropriate governance and risk management practices to manage identified climate-related risks; and that financial institutions remain financially resilient through severe, yet plausible, climate risk scenarios, and operationally resilient through disruption due to climate-related disasters.[16] The guideline should be clear that disclosure of climate-related risk management and transition plans must be embedded in financial reporting and subject to officer certification and independent third-party assurance. The financial institution should report information that is clearly defined, collected, and recorded; disclosing clear, balanced, and understandable information. Scenario analyses should be based on data used for investment decision-making and risk management.

The CCLI submits that Alberta's guidance should require financial institutions to disclose Scope 1, 2, and 3 greenhouse gas (GHG) emissions (absolute basis) on a phased-in basis; disclose the standard used to calculate and disclose the emissions; and if the reporting standard used is not the GHG Protocol Corporate Standard, disclose how the reporting standard is comparable with the GHG Protocol Corporate Standard.[17] We appreciate that Scope 3 data will initially be challenging to assess and may initially have to be estimated; however, considering that Scope 3 emissions comprise the majority of end-to-end carbon emissions, it will be important to estimate, particularly for projects in which the credit union provides debt or equity financing. For financed, facilitated, and insured Scope 3 GHG emissions, the financial institution should use the latest Partnership for Carbon Accounting Financials (PCAF) Global GHG Accounting and Reporting Standard for the Financial Industry (PCAF Standard), and if the reporting initiative used by the financial institution is not the PCAF Standard, then disclose how the reporting initiative used is comparable with the PCAF Standard.[18] The financial institution should describe the targets it uses to manage climate-related risks and opportunities and the financial institution's performance against these targets. These requirements would align with OSFI's Guideline B-15.

Adoption of a guideline for provincially-regulated financial institutions would align with ASFI's seven key supervisory principles to risk assessment, specifically:

[15] Guideline B-15, note 10 at 4-6.
[16] Guideline B-15, note 10 at 2.
[17] Guideline B-15, note 10 at 16.
[18] Guideline B-15, note 10 at 16.

1. Focus on identifying risks that are material to a regulated entity that may hold the potential for loss to the ARFI, depositors, clients, or the deposit guarantor.
2. Forward-looking, early, and timely intervention by ASFI where corrective action is warranted to resolve concerns.
3. Risk assessment that relies on sound, predictive judgment based on a clear and supported rationale.
4. Understanding the drivers of material risk to the regulated entity, including the entity's business model and operating environment, and understanding how risks may develop and how severe they may become in order to facilitate early identification of significant issues.
5. Risk assessment requires differentiation between the risks inherent to the activities undertaken by the regulated entity, and the regulated entity's management of those risks at both operational and oversight levels.
6. Risk assessment is continuous and dynamic to ensure that changes in risk, arising from both the financial institution and its external environment, are identified early.
7. Consolidated assessment of risks associated with the whole Institution in terms of capital and liquidity.[19]

The ASFI has stated that its supervisory framework is intended to align with regulatory and supervisory practices carried out by OSFI for federally-regulated financial institutions, where possible, recognizing that oversight may periodically differ based on Alberta's circumstances.[20] It is therefore timely that it issues aligned guidance on climate risk management.

The CCLI supports a prudential framework that recognizes the importance of Alberta-regulated financial institutions building financial resilience against intensifying climate-related risks in each aspect of their business plans. We note that OSFI's Guideline B-15 aligns with the framework recommended by the Financial Stability Board's Taskforce on Climate-related Financial Disclosures (TCFD)[21] and the International Financial Reporting Standards (IFRS) Foundation's International Sustainability Standards Board (ISSB) S2 Climate-related Disclosures,[22] which will ensure Canada keeps pace with regulatory developments for financial institutions globally. The embedding of oversight and management of climate-related risks and opportunities in governance, strategic planning, risk management, targets, and metrics will reduce risks of credit union or other financial institution failure from the growing frequency and intensity of acute events and the longer-term risks of chronic impacts.

Recommendation 2: Endorse the Sustainable Finance Action Council's proposed Green and Transition Finance Roadmap and co-operate as a member of the proposed Taxonomy Council's Indigenous, Provincial and Territorial Government Stakeholder Advisory Group in advising the Taxonomy Council.

A green and transition finance taxonomy is key to Canada's transition to sustainable finance as it will set standards for climate-related financial instruments and benchmarking climate risk management. The Alberta government can take a leadership role in endorsing the Sustainable Finance Action Council's (SFAC) proposed Green and Transition Finance Roadmap.[23] Several Albertan representatives participated in

[19] Alberta Superintendent of Financial Institutions - Supervisory Framework - January 2017 at 6-7.
[20] Financial institutions – Regulatory framework | Alberta.ca
[21] Financial Stability Board's Task Force on Climate-Related Financial Disclosure (TCFD) Framework.
[22] International Financial Reporting Standards (IFRS) Foundation, International Sustainability Standards Board (ISSB), S2 Climate-related Disclosures (2023).
[23] Sustainable Finance Action Council (SFAC) Taxonomy Roadmap Report (2022) (Taxonomy Roadmap).

working groups and steering committees to develop the taxonomy, and input from Albertan financial institutions and representatives from oil and gas companies has helped make the roadmap practical and feasible. The federal government in its 2023 Fall Economic Statement announced that the Department of Finance will work in consultation with regulators, the financial sector, industry and independent experts, to develop a taxonomy that is aligned with reaching net zero by 2050.[24] Alberta should participate as a member of the proposed Taxonomy Council's Indigenous, Provincial and Territorial Government Stakeholder Advisory Group in advising the Taxonomy Council as it moves forward.

A taxonomy is primarily a classification system – it outlines a common set of definitions and criteria to create clarity and agreement on what constitutes a "green" or "transition" investment. Taxonomies are a critical tool for solving two urgent and interrelated challenges within Canada's financial system: the ability to attract global capital to invest in Canada's low-carbon transition and to reduce the risk of greenwashing.[25] The fundamental role of the Taxonomy will be to create the market clarity and integrity necessary to accelerate capital investment into sustainable assets and projects. Investors need transparency and clarity in order to make strategic investment decisions. A taxonomy does not dictate investors' or companies' investment or capital expenditure choices.

A science-based taxonomy will create the market integrity, clarity, and interoperability necessary to accelerate global capital investment in Canada's low-carbon transition. The SFAC recommendations need to be implemented to facilitate company-level net-zero target setting, transition planning, and effective climate disclosure; evaluate projects against framework criteria to determine whether they are "green" or "transition"; and assess projects against "do no significant harm" criteria. The proposed Taxonomy will flow capital to decarbonization opportunities across all major emitting sectors. Alberta has an important role in helping to develop the Taxonomy in a manner that protects the safety and soundness of the financial system, aligning with ASFI's seven key supervisory principles to risk assessment noted above. What is important is that the Taxonomy Council's governance is evidence-based, transparent, independent, timely, and results focused.

Recommendation 3: Amend the Alberta Employment Pension Plans Regulation 154/2014 to require that the pension plan administrator's written statement of investment policies and procedures (SIPP) includes a statement on how its policies and procedures address climate-related financial risks, including the plan's climate resilience (mitigation and adaptation) and how it weighs the risks and benefits in decisions with respect to its portfolio of investments and loans, in light of the impending transition to a net-zero emissions economy.

It is vitally important that pension plans understand how climate risk impacts their portfolio from a risk adjusted returns perspective. A pension plan should expect its investment manager to report on the fund's carbon footprint, climate value at risk assessment under different scenarios, and the investment manager's strategy to address climate risk and opportunity.

The Alberta *Employment Pension Plans Act (EPPA*)[26] currently requires that the pension plan administrator ensures that the pension plan has a SIPP that meets the prescribed criteria in respect of the plan's portfolio of investments and ensures that the pension fund is invested in accordance with the SIPP established.[27]

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[24] Deputy Prime Minister Freeland, 2023 Fall Economic Statement, (21 November 2023), at 63, FES-EEA-2023-en.pdf (canada.ca).
[25] Taxonomy Roadmap, note 23.
[26] Alberta *Employment Pension Plans Ac*t, Statutes of Alberta, 2012 Chapter E-8.1, as amended *(*Alberta *EPPA).*
[27] Sections 37(2), 43(1) and (2), Alberta *EPPA*, note 26. See also section 42, Administrator must ensure governance policy established.

Section 54 of the Employment Pension Plans Regulation 154/2014[28] pursuant to the *EPPA* requires that the SIPP is established having regard to all factors that may affect the funding and solvency of the plan and the ability of the plan to meet its financial obligations, including categories of investments, diversification and liquidity of the investment portfolio; asset mix, including by reference to volatility and rate of return expectations; and other key factors to which the administrator had regard when establishing the SIPP. The CCLI submits that Alberta should amend the Employment Pension Plans Regulation to require that the pension plan administrator's SIPP also includes a statement on how its policies and procedures address climate-related financial risks, including the plan's climate resilience (mitigation and adaptation) and how it weighs the risks and benefits in decisions with respect to its portfolio of investments and loans, in light of the impending transition to a net-zero emissions economy. The CCLI recommends that section 54 be amended to require that Alberta-regulated pension plan administrators' SIPP includes a statement on how its policies and procedures address climate-related financial risks, including the plan's climate resilience (mitigation and adaptation) and how it weighs the risks and benefits in decisions with respect to its portfolio of investments and loans, in light of the impending transition to a net-zero emissions economy.

Pursuant to the Alberta *EPPA,* the pension plan administrator has a fiduciary duty in relation to plan members and beneficiaries, and the administrator must act honestly, in good faith, and exercise the care, diligence, and skill that a person of ordinary prudence would exercise when dealing with the property of another person.[29] That duty includes conducting effective risk management to advance plan objectives and protect plan assets from adverse risks. Investments must be made in accordance with the *EPPA* and in the best financial interests of plan members and beneficiaries; pension plan assets must be invested in a manner that a reasonable and prudent person would adopt if investing the assets on behalf of a person to whom the investing person owed a fiduciary duty to make investments, without undue risk of loss, and with a reasonable expectation of a return on the investments commensurate with the risk.[30]

The duty of impartiality requires trustees and fund managers to balance intergenerational interests in determining short and long-term investments. In order for pension fiduciaries to fulfill their fiduciary duty to act prudently, clear baseline standards with respect to climate governance and risk management are required, including identification, oversight, and management of climate-related risks and opportunities material to the financial risk-return profile of the pension fund's investments in the transition to a net-zero emissions economy. The amendment would align Alberta pension fund investment policies with OSFI's Guideline B-15 on Climate Risk Management for financial institutions and enhance Alberta's supervision of 653 pension plans with $57.4 billion in assets covering almost 300,000 members.[31]

We look forward to discussing these issues with you.

Sincerely,

Janis Sarra

Dr Janis Sarra,
On behalf of the Canada Climate Law Initiative

c. Sonia li Trottier, Director, CCLI, trottier@allard.ubc.ca

[28] Employment Pension Plans Regulation, Alberta Regulation 154/2014, sections 46(1), 54, pursuant to the Alberta *EPPA*, note 26.
[29] Sections 35(1) and (2), Alberta *EPPA*, note 26.
[30] Section 62, Alberta *EPPA*, note 26.
[31] Pensions Annual Statistics, note 7.