THE TASKFORCE ON NATURE-RELATED DISCLOSURES RELEASES ITS FINAL RECOMMENDATIONS TO POSITION NATURE RISK ALONGSIDE FINANCIAL, OPERATIONAL AND CLIMATE RISK

All too often, when we think of the resilience of the planet, we tend to think of climate. There is, however, an equally important component to that resilience, namely nature and biodiversity, and like climate in the throes of an existential crisis, nature is deteriorating globally, and biodiversity is declining faster than at any time in human history. The continued degradation of our life-sustaining ecosystems poses threats to societies and to business, including societies' ability to mitigate and adapt to climate change.

And all too often, the business world thinks of nature as unlimited and an endless source of critical inputs for operations and the value chains on which those operations depend. As David Craig, Co-Chair of the Taskforce on Nature-related Financial Disclosures ("TNFD"), noted in an interview in the Financial Times with Gillian Tett ("Our economic system is completely dependent on nature" – March 2023), financial systems need to identify and value risk, but they assume that the "natural system is free. It costs nothing to destroy a forest. It costs nothing to use as much water as you want, or to pollute. Therein lies the problem. So, we've got to, in effect, change the valuation, pricing and risk approach within financial markets to make sure that we put a value on the natural system."

Because the climate emergency attracted early attention and vocal advocacy, aided in part by a tangible (albeit potentially elusive) goal of limiting the increase in global warming to 1.5˚C, protection of far more complex nature and biodiversity ecosystems, not to mention the integral role these ecosystems can play in protecting against climate change, did not command the attention it deserved. That is now changing. As part of the effort to bring nature into the sustainability conversation, the TNFD is dedicated to responding to nature risks, in the same way a slew of standard-setters did for climate (what Craig characterizes as "two sides of the same coin"), namely seeking to redirect capital to nature-positive outcome, based on corporate disclosure.

Why Business Needs to Care About Nature Risk

According to World Economic Forum research ("Nature Risk Rising: Why the Crisis Engulfing Nature Matters for Business and the Economy," January 2020), $44 trillion of economic value generation (over half the world's GDP) is moderately or highly dependent upon nature and its services. Together, the three largest sectors that are highly dependent on nature generate close to $8 trillion of gross value added: construction ($4 trillion); agriculture ($2.5 trillion); and food and beverage ($1.4 trillion). This is roughly two times the size of the German economy. In addition to the more obvious risks to primary industries, the consequences for secondary and tertiary sectors can also be significant.

Nature risk can be material for businesses, according to the WEF, in multiple ways:

- when businesses depend directly on nature for operations, supply chain performance, real estate asset values, physical security and business continuity;
- when the direct and indirect impacts of business activities on nature loss can trigger negative consequences, such as losing customers or entire markets, legal action and regulatory changes that affect financial performance; and

- when nature loss causes disruption to society and the markets within which businesses operate, which can manifest as both physical and market risks.

This landscape should put into perspective why it is imperative that we halt and reverse nature loss and find ways to live in greater harmony with nature. A key part of that is to close a $4.1 trillion financing gap by 2050.

With six of the nine planetary boundaries (processes critical for maintaining the stability of the Earth) already breached, risk to the resilience of ecosystem services from nature on which communities survive and on which businesses depend to generate cashflow and returns (separate and apart from climate risk) has become a financial risk. Said another way, nature-risk is embedded in corporate cash flows and capital portfolios. And although global executives rate biodiversity loss and ecosystem collapse at the top of the risk register, these are the risks that we seem to be least prepared to address. Experts posit that investors, lenders and businesses have yet to fully appreciate their nature-related dependencies, impacts, risks and opportunities, and thus are failing to adequately account for nature in strategic decisions and capital allocation.

The TNFD Recommendations

One initiative to help business and financial institutions meet the challenge of incorporating nature into decision-making is the TNFD.[1] The TNFD recognizes that nature needs to be addressed as a core and strategic risk management issue, alongside climate change, and that nature needs to be brought into strategy, risk management and capital allocations decisions, with nature being fully integrated with climate considerations. In contrast though to the fight against climate change, for which GHG emissions are easily measured, nature is, as David Craig pointed out, "far more complex and interrelated." TNFD seeks to "break down that complexity" and meet head on the excuses for doing little to grapple with nature because the problem is too complex for financial markets to absorb.

The final recommendations of the TNFD, which are intended to provide businesses and financial institutions with a disclosure and risk management framework to identify, assess, respond to and disclose, nature-related issues, and thereby contribute to the shift in global capital flows towards nature-positive outcomes, were released in September. Concurrently, the TNFD also issued implementation guidance. The recommendations consist of 14 sets of disclosures across the four pillars: governance, strategy, risk and impact management, and metrics and targets. (I first described these efforts in a March 2022 briefing note.)

The TNFD recommendations build on the language, structure and approach of the Taskforce on Climate-related Financial Disclosures ("TCFD") (*see* my November 25, 2021 Climate Lexicon), and are consistent with the ISSB's IFRS S-1 Standard (*see* my June 28, 2023 briefing note). TNFD Recommendations are also aligned with the requirements of Target 15 of the Kunming-Montreal Global Biodiversity Framework for corporate reporting, which calls for assessment and disclosure of nature-related risks, impacts, and dependencies,

[1] The TNFD initiative was led by 40 Taskforce members representing over US$20 trillion in assets under management, and has drawn on the support and active input of market and non-market stakeholders from almost 60 countries.

enabling companies now to align their corporate reporting with global policy goals as they are doing on climate-related issues.

The TNFD will now encourage and support voluntary market adoption of its recommendations. The toolkit includes, among others, sets of additional guidance to help businesses and financial institutions identify and assess nature-related issues and inform disclosure:

- Getting started with adoption of the TNFD recommendations;
- Guidance on the identification and assessment of nature-related issues;
- Discussion paper on proposed sector disclosure metrics;
- Guidance on scenario analysis;
- Guidance on specific types of ecosystems (biomes)
- Discussion paper on proposed approach to value chains; and
- a Glossary.

Concluding Thoughts

Ultimately, the TNFD disclosure effort, like the TCFD disclosure effort, is about channelling capital flows in support of a sustainable future. While TCFD is focused on a related, but ultimately separate disclosure issue, climate, TNFD is focused on nature and environmental risks that stem from degradation of ecosystems and loss of biodiversity. The approaches to disclosure are, not surprisingly, similar, and TNFD has gone to great lengths not to reinvent the wheel, but rather to build on the TCFD model, and to fit within the ISSB standards, and the materiality approach used by the Global Reporting Initiative and incorporated into the new European Sustainability Reporting Standards (*see* my August 6, 2023 briefing note). This is intended to allow enterprises across jurisdictions, with their varied approaches to materiality, to follow a single set of recommendations.

While the disclosure focus on climate and nature are separate, reaching sustainable outcomes means recognizing that climate and nature are interlinked and that to get to net-zero, nature-based solutions and nature systems will be critical. As many learned with carbon and climate, one needs to start with awareness, and that in turn requires information. Perhaps too, the broader focus on environment (and seeing climate as a subset of nature) may allow people to move past the polarization that climate debates engender. After all, it is far easier to grasp the destruction of a forest or the pollution of waterways than it is to grasp the relationship between carbon and the consequences of global warming.

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Washington, D.C.
October 14, 2023