Business

Canadian banks need to start thinking about how to manage climate risk, report says

Tuesday, October 25, 2022 @ 2:40 PM | By Ian Burns

Share Print Tweet Email

A legal think tank is saying the directors of Canadian banks need to start taking a good look at their strategies for helping to mitigate climate change and move toward a net-zero economy, or they may be putting themselves at risk.

The new report from the Canada Climate Law Initiative (CCLI), *Banking on a Net-Zero Future: Effective Climate Governance for Canadian Banks*, is aimed at providing a comprehensive guide to the current state of the law, the risks and opportunities associated with climate change for the financial sector, best practice guidance on oversight and governance, and a snapshot of the kinds of decisions bank boards are making on their pathway to net-zero emissions.

Under the *Bank Act*, directors have duties to act honestly, in good faith, and with care, diligence, prudence and skill, with a view to the best interests of the bank. And those duties require directors to have effective oversight of the bank's management of climate change, according to the CCLI.

There has been a dramatic shift in expectations of Canadian banks to manage climate risk and make capital allocation decisions based on greenhouse gas emissions, the CCLI said.

Janis Sarra, Canada Climate Law Initiative

The Initiative's principal co-investigator, Janis Sarra, said a major expectation is the idea that banks should be using their capacity to allocate capital to meet Canada's domestic and international commitments to get to net-zero emissions and should take ownership of greenhouse gas emissions associated with their investments and lending activities, which are referred to as "financed emissions."

"Previously banks were being scrutinized by investors and other stakeholders about how they are reducing their own emissions, but their own emissions are only a tiny fraction of what they have control over," said Sarra, a law professor at the University of British Columbia. "Banks are regulated as public entities, and they are regulated in a special way because the safety and soundness of our financial system, so they have obligations as a result of that to take a serious look at their financed emissions."

Sarra said most the risks faced by banks are transition risks, which are associated with regulatory change, market changes and litigation.

"They have some risks in the sense that if there are acute events like the atmospheric rivers in British Columbia last year, their services are interrupted, and they may have damage to structures and the real estate they own. But the transition risks are really where the issues are," she said. "So, if they don't have a vision, or engage in effective governance, there is a risk down the line that a number of their assets will be stranded — and that would create capital adequacy problems for banks, which in turn could affect the interests of deposit holders and other investors."

The guide noted making decisions regarding capital allocation is a complex one for banks operating in a resource-rich economy, and a transforming economy creates risk and opportunities for banks that must be taken into account in establishing the strategy of the bank and managing the risk — which requires effective board oversight.

The CCLI said banks need to adapt and adjust as governments act, which requires strong governance, risk management and strategic planning. Banks need to provide leadership in facilitating the flow of finance to support businesses in reducing their emissions "through the proactive design of products and services that facilitate a just transition for communities suffering the most serious impacts of acute physical events and facing the greatest transition risks," the guide said.

"This guide will support bank directors as they work with their executives to develop strategies to transition the bank's operating and financed emissions towards net-zero and will assist institutional investors and other stakeholders in their engagement with bank boards on these important issues," said Catherine McCall, executive director of the Canadian Coalition for Good Governance.

Sarra noted there has been an "exponential increase" in litigation surrounding climate change, and the ones which have been brought against financial institutions are largely by investors who want greater transparency by banks in terms of what they are doing about their financed emissions, and whether they are overemphasizing the finance of high carbon intensive sectors. Another litigation risk is associated with "greenwashing," where a company makes claims that lead consumers to think they are doing more for the environment than what is actually true.

"There was a recent decision in the U.K. in regard to HSBC and poster ads talking about sustainable financing and how they were planting trees," she said. "And the advertising regulator said they were leading the public to believe they were making an overall improvement in the transition to net-zero, and they were not. That is pretty big reputational damage to that bank."

The Canada Climate Law Initiative (CCLI) provides businesses and regulators with climate governance guidance so that they can make informed decisions in the transition to a net-zero economy. More information can be found here.

If you have any information, story ideas or news tips for The Lawyer's Daily please contact Ian Burns at Ian.Burns@lexisnexis.ca or call 905-415-5906.

Related Articles

- Bill C-12 can demonstrate environmental leadership to Canadian business | Janis Sarra
- New report offers retail company directors guidance on how to deal with climate change risks
- Three reasons why lawyers should engage with climate change | Meredith James and Aladdin Diakun
- Business, government need to be aware of risks associated with fossil fuel subsidies: report
- Time for boards to stop greenwashing, get serious about net-zero carbon

Featured

 SCC's fall session features weighty immigration, tort, family and tax appeals

Latest

Criminal Senior Crown Attorneys, Society of United Professionals announce shared services agreement
Judicial Appointment Anick Pelletier appointed judge of the Tax Court of Canada
[Legal Wire] Ontario court adopts new test for opting out of class actions post-deadline
[Legal Wire] Ontario cannabis company to pay OSC $1.4 million for accounting errors
Real Estate Ontario proposes legislation to build 1.5 million homes in next 10 years, supports 'gentle density'

News | SCC | Business of Law | Digests | Insider | Opinion | Analysis | Legal Innovation | Access to Justice | COVID-19

LexisNexis may contact you in your professional capacity with information about our other products, services and events that we believe may be of interest. You can manage your communication preferences via our Preference Centre or via the unsubscribe link provided within our communications. You can learn more about how we handle your personal data and your rights by reviewing our Privacy Policy.

Thank You!