



ESTABLISHING CHINA'S GREEN FINANCIAL SYSTEM

Detailed Recommendations 14: Make Environmental Information Disclosure Mandatory



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Detailed Recommendations 14:

Make Environmental Information Disclosure Mandatory

With growing environmental problems on a global scale, corporate disclosure of environmental information has drawn growing attention from the public. Disclosure of environmental information intends to reveal the impacts of various corporate activities on the environment. In the mid-1980s, the environmental information of listed companies and bond issuers of overseas capital markets mainly appeared in the 'management discussions and analysis' (or board meeting reports) and later became an independent component of annual reports before further evolving into a separate environmental report aside from corporate annual report (or otherwise referred to as CSR report or corporate sustainability report).

China has already initiated relevant activities for environmental information disclosure and initially put into place a system of rules (see Table 1). Environmental information disclosure comprises two components, including temporary public announcements and regular reports. The former mainly refers to the disclosure of material environmental information by listed companies, including major potential impacts of newly introduced environmental laws, regulations, rules and industry policies on companies, investigations of environmental authorities on companies for environmental violations or the imposition of criminal or major administrative penalties. Given the nature of 'materiality', such information is subject to compulsory information disclosure and required to be disclosed by listed companies in a timely manner (for instance, disclosure of major environmental incidents shall be made within two days as of the day of an incident's occurrence).

Environmental information disclosure of regular reports can be divided into the following circumstances: first, listed companies and their subsidiaries in heavy pollution industries identified by state environmental protection authorities shall disclose major environmental issues and rectification status, emissions of major pollutants in compliance with standards, construction and operation of corporate environmental facilities, emergency response plan for environmental pollution incidents and comparison of environmental protection parameters of the same industry during reporting period in accordance with the *Law on the Promotion of Cleaner Production and Measures for the Disclosure of Environmental Information* (Trial Implementation). Second, other general enterprises are encouraged by regulatory departments and exchanges to proactively disclose their CSR performance including their measures taken in such areas as pollution control, ecological protection, the maintenance of social security, and achievement of sustainable development. Environmental report and sustainable development report should be disclosed on an annual basis. In practice, the environmental report of listed companies is often disclosed together with annual report within four months after the end of a fiscal year.

In recent years, listed companies have been releasing an increasing number of CSR and environmental reports. According to the *Securities Times*, by April 30, 2014, a total of 674 companies listed on Shanghai and Shenzhen stock markets disclosed 686 CSR reports for 2013 (including sustainability reports and environmental reports), which account for 26.57 percent of all listed companies. Most companies have disclosed their environmental protection policies and the performance of such policies.

Table 1: Major regulations on environmental information disclosure

Name of regulations and circulars	Issuing authority	Year of promulgation
<i>Administrative Measures for the Information Disclosure of Listed Companies</i>	CSRC	2007
<i>Measures for the Disclosure of Environmental Information (Trial Implementation)</i>	The former State Environmental Protection Administration (SEPA)	2008
<i>Opinions on Enhancing the Supervision and Management on the Environmental Protection by Listed Companies</i>	The former State Environmental Protection Administration	2008
<i>SSE Guideline on Environmental Information Disclosure by Listed Companies</i>	Shanghai Stock Exchange	2008
<i>Guidelines for Environmental Information Disclosure by Listed Companies (Consultation Draft)</i>	The Ministry of Environmental Protection	2010
<i>Social Responsibility Instructions to Listed Companies, Standard Operation Guidelines for Listed Companies</i>	Shenzhen Stock Exchange	2006 2010

(I) The case for environmental information disclosure

With the global flow of capital and growing international corporate competition, tendencies of information disclosure in overseas markets deserve our attention. With the deepening of China's economic transformation and restructuring, the importance of information disclosure will become even more striking.

1. Compulsory or partial compulsory environmental information disclosure is a common international practice

The United Nations, the US, the EU and Japan are the early movers of environmental information disclosure. Today, compulsory or semi-compulsory requirements on the environmental information disclosure by listed companies have already become a common practice in the developed world. The Netherlands is the earliest European country that adopted the practice of environmental information disclosure, which includes corporate environmental policy, management system, product testing and environmental monitoring measures, and such data shall be externally audited. Japan did not require environmental information disclosure until the late 20th century but has been moving rapidly and leads Asia today. In the US, environmental information disclosure emerged sporadically in the 1970s. Among those efforts of corporate environmental information disclosure, the US Congress, the Environmental Protection Agency, the Financial Accounting Standard Board (FASB) and the Securities Exchange Commission (SEC). In 2012, the Hong Kong Securities and Futures Commission has identified Environmental, Social and Governance Reporting Guide as a recommended regular requirement and plans to elevate certain recommended disclosure responsibilities into a requirement whose non-compliance requires an explanation by no later than 2015. Of the 55 member exchanges of the World Federation of Exchanges, more than a third have released sustainability reports or guidelines, or have held training sessions on this subject for companies. In particular, 12 exchanges require at least a subset of the listed companies to furnish social and environmental reports (i.e. partial mandatory disclosure), 7 of these require all companies to make such disclosures (i.e. mandatory disclosure).

2. Environmental information disclosure by listed companies and bond issuers help the market better conduct risk evaluation and can be used by the public/NGOs to exert pressure on polluting companies

Information disclosure is a fundamental system for stakeholders including investors to assess corporate value and risks. With the growing importance of environmental issues, corporate environmental information, including environmental policy, major pollutants, mitigation measures and pollution control effects, has increasingly become an important basis for corporate evaluation, risk assessment, and investment and purchase decision-making by creditors, investors, communities and even consumers. Meanwhile, open and transparent environmental information disclosure also enables the public, investors and NGOs to create pressures on polluting companies.

3. Environmental information disclosure by Chinese listed companies has already taken initial steps but needs to improve

As mentioned above, China's environmental protection authorities, securities regulatory institutions and securities exchanges have already introduced a set of rules and guidelines for environmental information disclosure by listed companies and a growing number of listed companies have started to disclose their environmental information. Nevertheless, most information disclosure has so far been made mainly on a voluntary basis without compulsory requirements; in addition, the following problems have also emerged, including the imbalance of environmental information disclosure, excessive definitive description, insufficient information transmission and lack of details. These problems have limited the market assessments of

corporate environmental value and risks and compromised the functioning of market mechanisms for environmental information evaluation, supervision and index product development.

There are almost no requirements on the environmental information disclosure by bond issuers and the market lacks sufficient information to assess the probability for the occurrence of pollution violations by bond issuers and consequent risk level, where rules need to be further improved.

(II) Recommendations for environmental information disclosure by listed companies and bond issuers

1. Development of compulsory rules on environmental information disclosure

The 12th Five-Year Plan (2011-2015) explicitly requires an enhanced awareness of the urgent need for and establishment of green and low-carbon development concepts in the face of growing constraints on resources and the environment. It also calls for the perfection of incentives and disincentives with the priority of energy conservation and emission abatement. The 18th CPC Report has called for “accelerating the development of a system of ecological civilization and systems and mechanisms for land development, resource conservation and eco-environment protection”. The newly revised Environmental Protection Law came into effect in January 2015 and includes relevant requirements on environmental information disclosure.

We suggest that the CSRC and the stock exchanges highlight the important value of corporate environmental information, identify environmental information as an indispensable element of corporate information disclosure, and formulate compulsory rules for environmental information disclosure. For instance, responsibilities for the disclosure of sustainability information in regular reports and interim reports should be prescribed by securities regulatory authorities in the administrative measures for information disclosure and guidelines for the format of regular reports and by exchanges through IPO rules and CSR disclosure guidelines and rules.

2. Require listed companies and bond issuers to disclose key information in accordance with disclosure standards

In addition to observing the basic principles for environmental authorities on environmental information disclosure, listed companies and bond issuers should disclose specific environmental information closely related to corporate performance as well. Thus, it is suggested that regulatory authorities promulgate compulsory requirements that listed companies and bond issuers provide quantitative disclosure of key information. The objective is to increase the materiality of information disclosure, avoid generalization, and enhance quantitative and comparable information disclosure in order to ensure effective utilization of data by the market and other stakeholders.

Compulsory environmental information disclosure by listed companies can be implemented in a step-by-step manner. For instance, in the short run, compulsory disclosure requirements can be imposed upon key polluters or (and) specific types of companies; in the middle term, the scope of

companies subject to compulsory disclosure will be expanded; and in the long run, compulsory disclosure requirements should be imposed on all companies.

Compulsory requirements of environmental information disclosure of bond issuers may also be implemented in a step-by-step manner. In the first step, financial institutions that issue green bonds can be compulsorily required to disclose environmental information. After certain experiences are gained, the scope of disclosure requirements can be extended to cover other bond issuers.

3. Give play to the role of intermediaries to evaluate, supervise, guide and incentivize environmental information disclosure

First, intermediaries should be encouraged to conduct an environmental credit rating for listed companies and bond issuers, and third-party authentication and ratings for environmental information disclosure. They should fully exploit the value of environmental information. Meanwhile, they should also be encouraged to reveal those companies with poor environmental performance and inadequate disclosure in order to enforce certain supervision and restraint. Second, considering the mandatory and voluntary disclosure of environmental information, various intermediaries may provide guidance and technical support in the form of best practices. Third, securities, index and investment institutions should be encouraged to develop and design various indices and products related to the environment to develop positive and negative feedbacks to corporate environmental information disclosure.

4. Enhance regulatory cooperation and enforcement of environmental information disclosure

Securities regulatory authorities, self-regulatory organizations and environmental protection departments should continue to enhance information sharing for corporate environmental information disclosure and further step up quality supervision of environmental information disclosure by listed companies and bond issuers, including the timeliness, reliability and comparability. Breaches of regulations on environmental information disclosure should be subject to penalties that are fully aligned with existing regulatory methods of information disclosure, with a view to promoting the transparency and openness of environmental information disclosure of listed companies and bond issuers.

In addition, the scope of compulsory environmental information disclosure can be expanded in a step-by-step manner to include more indicators into the scope of mandatory disclosure and impose relevant penalties on listed companies and bond issuers that refuse to fulfil their disclosure obligations to create certain constraints and pressures.

THE GREEN FINANCE TASK FORCE

The Green Finance Task Force was initiated by People's Bank of China (PBC) Research Bureau and the UNEP Inquiry into the Design of a Sustainable Financial System in 2014. The Task Force brought together leading Chinese financial policy and regulation experts together with experts from the private sector, academia and think tanks, as well as international experts.

A number of organizations have lent great support to this Task Force, chief among them are Chongyang Institute for Financial Studies of Renmin University, the Ecological Finance Research Center at the Renmin University of China, the Eco Forum Global, the International Institute for Sustainable Development, the Green Credit Special Committee of China Banking Association, and China Finance 40 Forum.

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