OECD
BETTER POLICIES FOR BETTER LIVES

The Supreme Audit Institutions: and Climate Change

Presentation to the

2024 ADB Regional Public Sector Accounting Forum

Peter Welch, Senior Advisor,

PMB/OECD

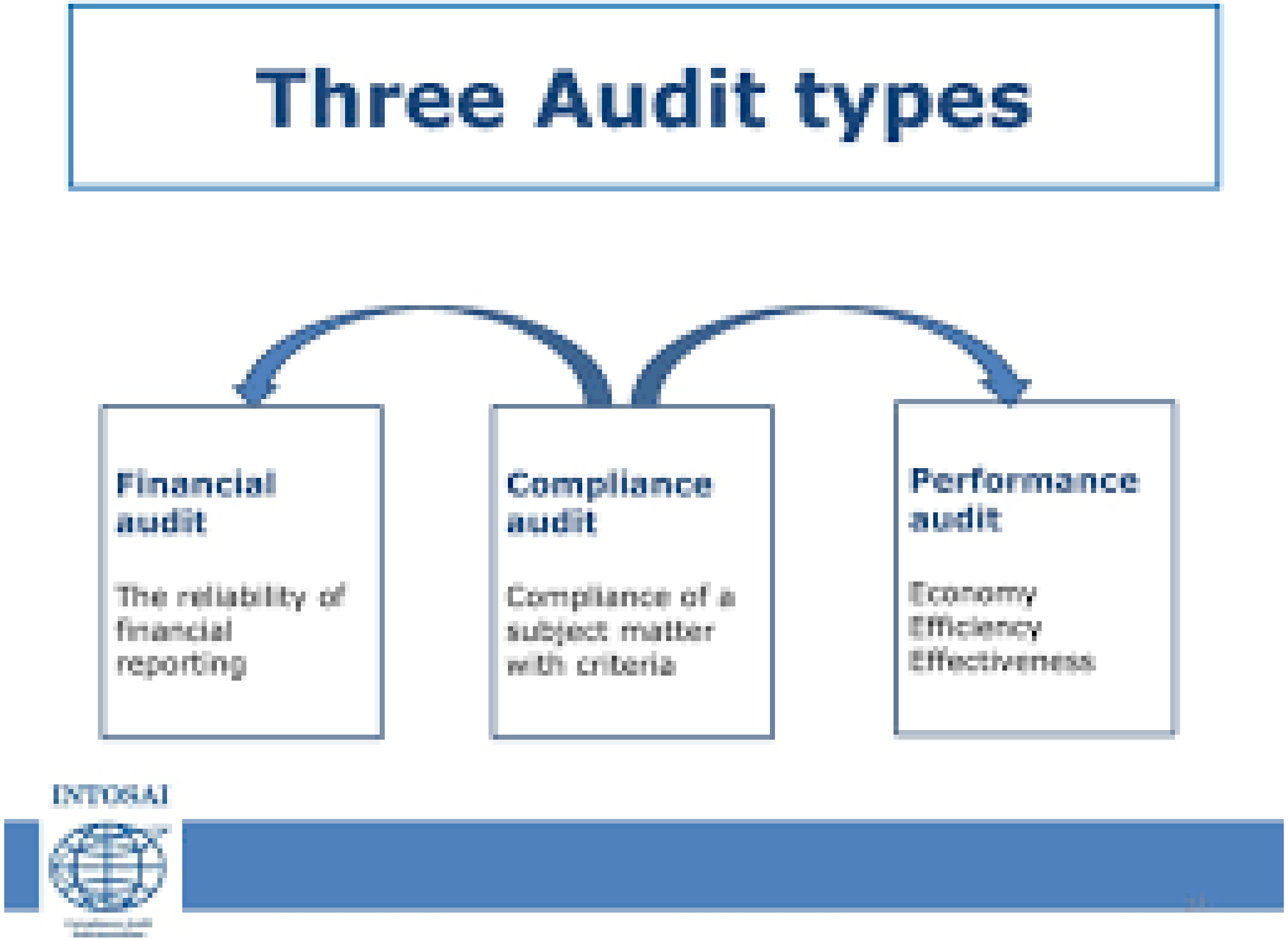
September 2024

Three audit types for supreme audit institutions?

Financial audit: on published information – general purpose financial statements, the annual report.

Compliance audit – is spending legal and regular? Have public servants followed the law in managing public resources? Anti-corruption role?

Performance audit – have public authorities used public resources in ways that are economic, efficient and effective? Have public authorities made good choices?



Peter Welch,

Senior Advisor,

PMB/OECD

Disclosures and levels of assurance…

Financial audit: on published information – general purpose financial statements, the annual report.

Reasonable assurance: the balance sheet, the income statement

Limited assurance: (simplifying) statements by management in the Annual Report. Currently, in most cases, this includes information on climate change.

Summary

- Some climate metrics for sovereign bond portfolios are currently affected by macroeconomic volatility, which complicates year-on-year comparisons. These metrics are therefore limited in their usefulness as measures of financial risk. For example, the fall in the Weighted Average Carbon Intensity (WACI) of the Bank's sovereign bond portfolios between February 2023 and February 2024 largely reflected the unwind of Covid-related impacts (due to data lags). And the material increase in Natural Resource Rents (NRR) of the Bank's sovereign portfolios reflects sharp increases in commodity prices.[29]
- Implied Temperature Rise (ITR) metrics for the Bank's sovereign bond holdings have remained stable and suggest that the Bank's sovereign bond holdings are aligned with the 2°C Paris goal, but not with the 1.5°C ambition. They remain lower than a G7 reference portfolio.
- In order to quantify the financial risks, to which its sovereign bond portfolios are exposed, the Bank continues to build out its scenario analysis capabilities. This analysis suggests that

Peter Welch,
Senior Advisor,
PMB/OECD

The context: The Paris Agreement, NDCs and the work of SAIs…

The legally binding nature of the Paris agreements gives SAIs a good basis to conduct audits on the action taken by their governments to reach the targets – which is to say **performance audits**. The Paris requires each Party to prepare, communicate and maintain successive nationally determined contributions (NDCs) that it intends to achieve. SAIs have good criteria for audits that seek to answer a popular question: are we on track?

SAIs are very active in looking at climate change issues – from a performance perspective

INTOSAI WGEA has 86 members

Essentially this exists to share ideas on performance audits

They are interested in both mitigation and adaptation

Peter Welch,

Senior Advisor,

PMB/OECD

AUDIT FINDINGS

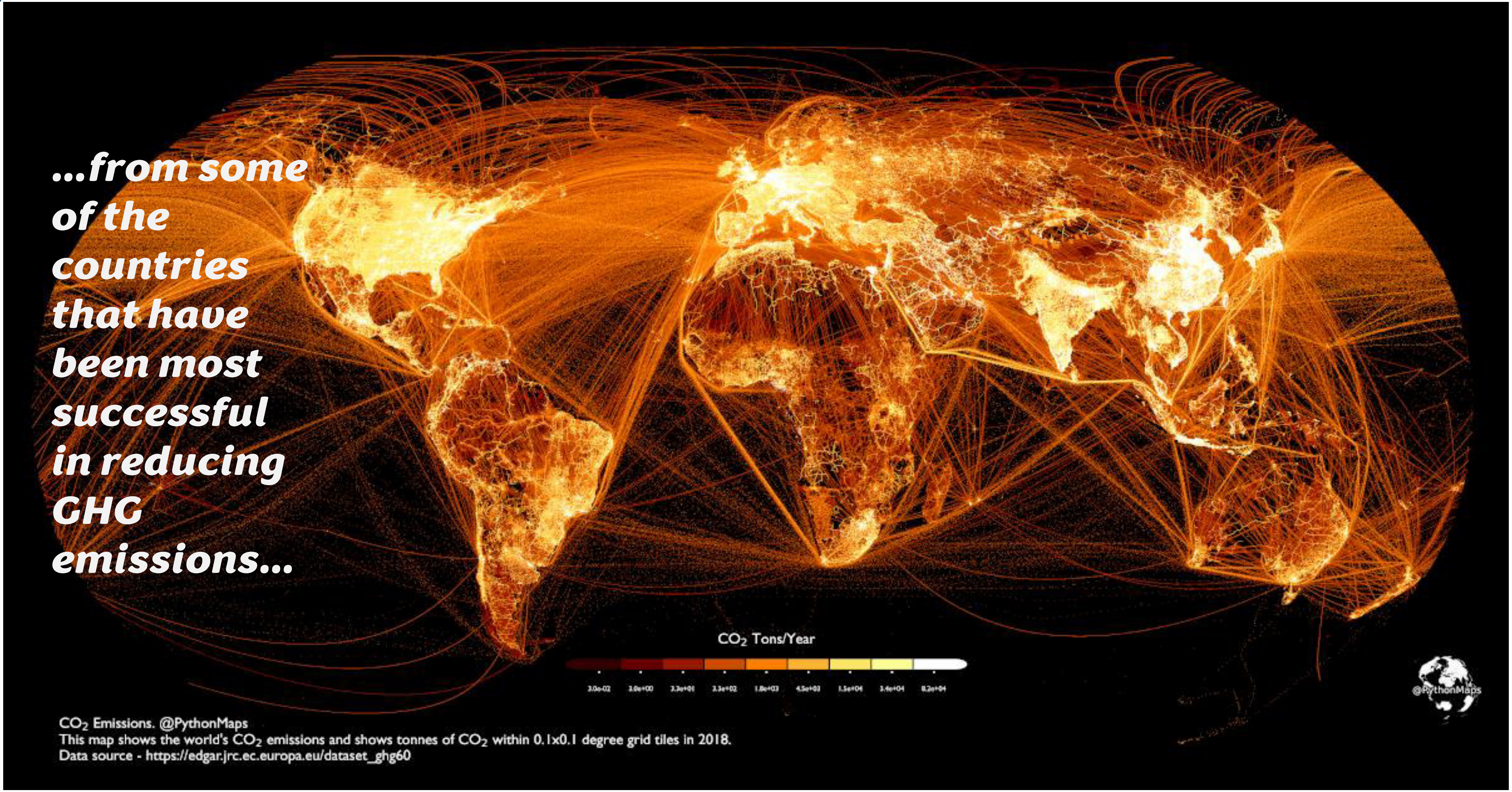
- Austria: Greenhouse gas emissions increased by 5% from 1990 to 2017, failing to meet reduction targets in 2017 and 2018. Different sectors showed varied performances against their targets.
- Canada: The carbon pricing system faced inconsistencies in emission coverage and weak requirements for large emitters. Despite measures to mitigate burdens on vulnerable groups, there was a lack of transparency in reporting.
- United Kingdom: The central government reported a 50% reduction in emissions by 2019-20 compared to the 2009-10 baseline, though the framework does not cover all public sector emissions and many scope 3 emissions.
- Cyprus: The effectiveness of the Emissions Trading System (ETS) varied, with power production emissions increasing by 6% since 2005. There is a need for robust databases and better monitoring
- Sweden: The greenhouse gas reduction mandate has increased biofuel use, but sustainability risks present challenges

Peter ...felch,

Senior Advisor,

PMB/OECD

SAIs analysis largely compares results to NDCs – not to other countries…



Some SAIs have focussed on mitigation efforts…

Austria. Weather and climate-related costs are projected to increase substantially. Need for better coordination and the formulation of precise and harmonized measures to address climate impacts effectively

Canada: There are gaps in the integration of climate resilience measures across various jurisdictions. The lack of consistent criteria for assessing the impact of climate policies on vulnerable groups is a significant issue

Colombia: Climate change impacts include glacier retreat, sea level rise, and coastal erosion. Future scenarios predict significant temperature increases and precipitation changes. The report calls for better coordination and comprehensive planning for effective adaptation.

France: The report underscores the urgency of adaptation, emphasizing significant financial investments needed. It stresses the importance of integrating climate change effects into various sectors and evaluating the adaptation of infrastructure and urban planning.

Peter Welch,

Senior Advisor,

PMB/OECD

The private sector seems to be further along the path to implementing TFCD

Private sector application of TFCD principles

- United States
- European Union
- Switzerland
- United Kingdom
- Japan
- etc

Public sector application of TFCD principles

- United Kingdom and New Zealand throughout government
- Financial Institutions and SOEs in most OECD member countries

Towards assurance…

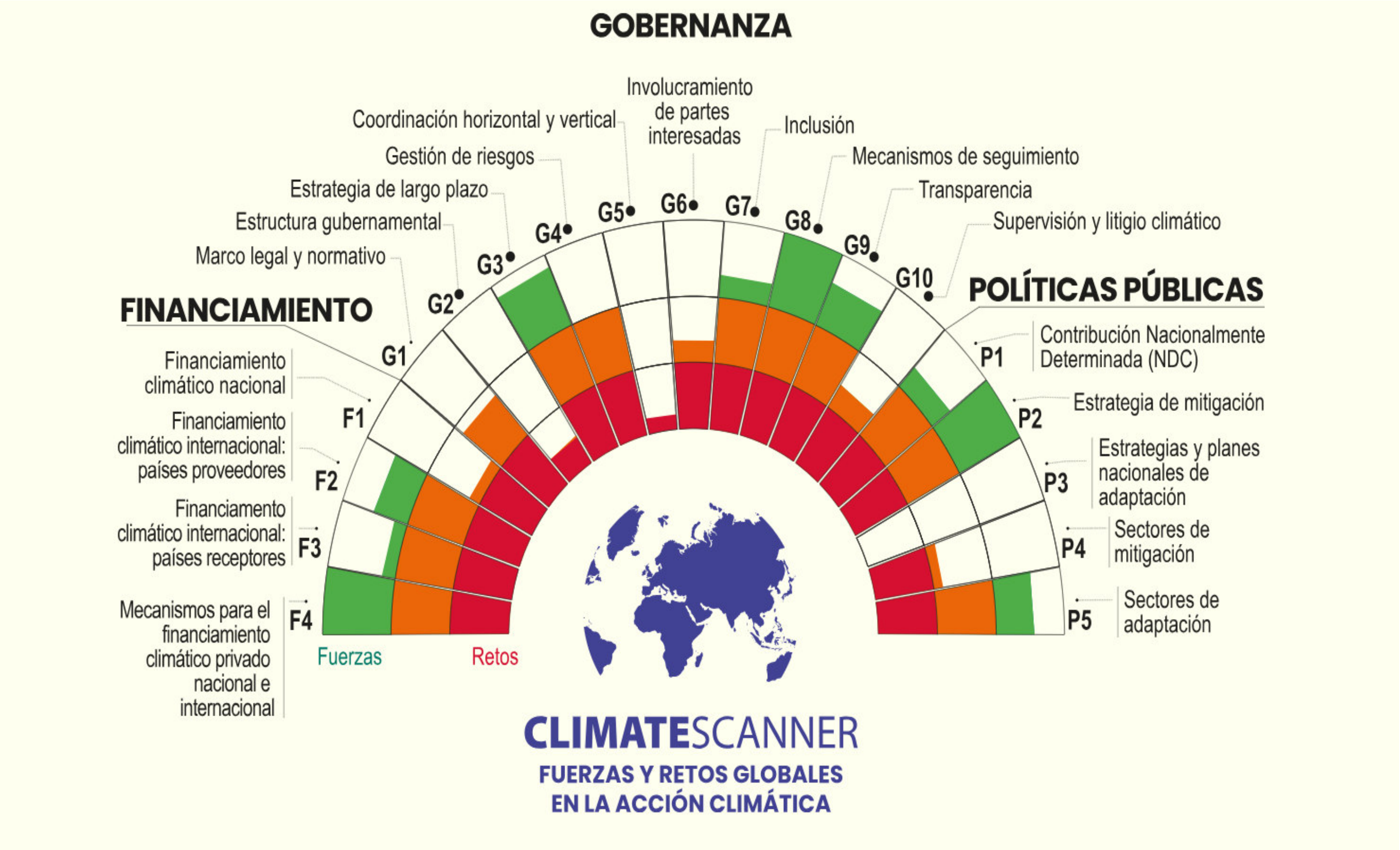
- Understand the context (see slide 5)
- Understand the business
- Review risks

Peter Welch,

Senior Advisor,

PMB/OECD

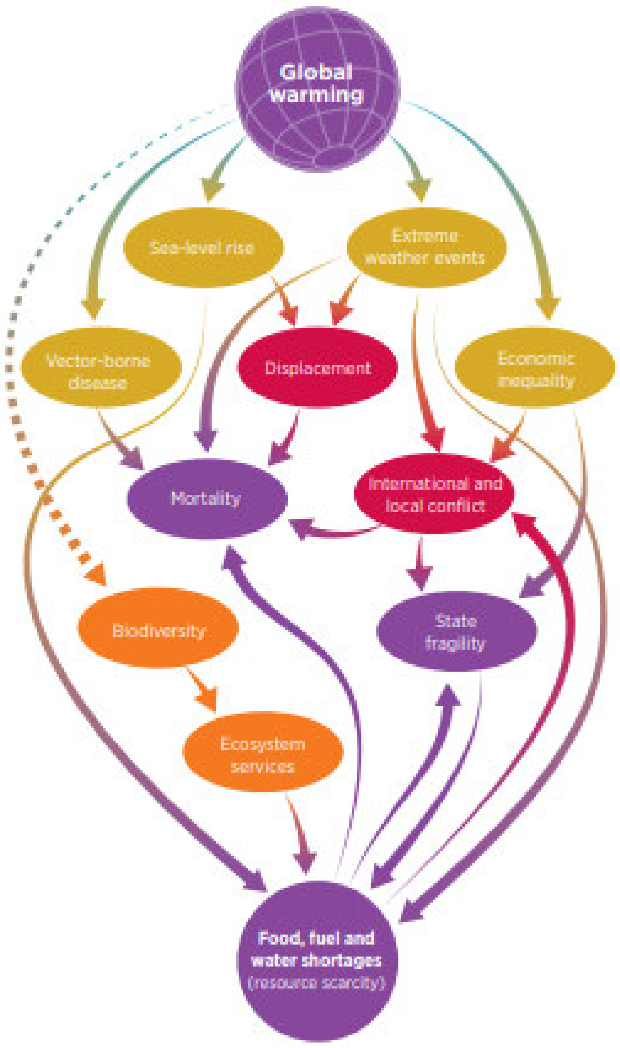
The INTOSAI Climate Scanner



A coordinated effort to understand the business at government level?

Understand the risks: ask an actuary?

Figure 8: Cascading global climate failure



Source: Kemp et al, 'Climate Endgame: Exploring catastrophic climate change scenarios' (2022). Licensed under CC by 4.0.

- They suggest that **the costs of Greenhouse Gas Emissions may exceed global GDP** well before the end of the century.
- And that **the impact on Global GDP is going to be very large before then** – notably because the impact of Extreme Weather Events on insurance.
- This contrasts with the forecasts reflected in many private sector disclosures at present.

… at what point do we expect 50% GDP destruction - somewhere between 2070 and 2090 depending on how you parameterise the distribution.

Use multiple sources of evidence

Complexity of Scope 3 Emissions

•These emissions arise from activities not directly controlled by the reporting body, making it difficult to verify the accuracy and completeness of the reported data.

Climate Risk Assessments

•. Auditors must evaluate how well bodies identify and quantify these risks, and how they impact future financial performance or GHG emissions.

Using Climate Scenarios, Estimates and Assumptions

•Climate and GHG disclosures often rely on estimates and assumptions, such as future emissions, the impact of climate policies, or the expected life of assets

Technological and Analytical Challenges

•Auditors will need to use advanced technologies and data analytics to verify GHG emissions data and assess climate-related risks. Data analysis will be a factor in comparing data from different sources.

• Conclusion

SAIs have already provided useful insights in climate change mitigation and adaptation – and can do more

The growth of climate change disclosures in annual reports and accounts means their role evolves and they need to learn more from each other.

The scale of damage from climate change – as outlined by the actuaries – means that climate change is on course to have a fundamental impact on public finances and the valuation of assets.

Peter Welch,
Senior Advisor,
PMB/OECD

Thank you!

Please ask me some questions!

Peter Welch, PMB/OECD **peter.welch@oecd.org**

Climate policies that achieved major emission reductions: Global evidence from two decades

Are rare: around 70 highly successful policy combinations in the 1500 OECD databases.

Most likely to work when there is a price signal – like a carbon tax.

It wouldn't even be enough to replicate the most successful policy mixes, **we would only be halfway** to our targets.

Backs up SAI conclusions on lack of coordination.