Chapter Zero New Zealand
The Directors' Climate Forum

Hosted by
Institute of DIRECTORS NEW ZEALAND

Transition planning

A guide for directors

Created with the
External Reporting Board
Te Kāwau Ārahi Pūrongo Mōwaho

XRB | Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

This guide has been prepared by the Institute of Directors (IoD) in New Zealand, as host of the Chapter Zero New Zealand directors' climate forum, in association with the External Reporting Board (XRB).

Our particular thanks to Chapter Zero New Zealand Foundation Partner KPMG for their input and advice in this work, Aurecon for graphic support to strengthen the messaging, and the members of the Chapter Zero NZ working group and governance and sustainability community that supported the development of this resource.

October 2024

Contents

Foreword

Transition planning supports the transformation of businesses. With the societal demand for tangible action on climate change, directors need to be transparent about climate action and develop and disclose credible plans for the transition to a low-emissions, climate-resilient economy. Transition planning can also be leveraged by businesses to embed other systemic risks into their long-term thinking, such as nature or social equity, that also interact with climate. It has wider benefits for businesses including supporting technological transformation, increasing productivity and enhancing long-term cost efficiencies.

This guidance is an introductory reference for directors of Climate Reporting Entities (CREs) as they commence transition planning but can also be used to support transition planning by the broader governance community.

Disclosures made under Aotearoa New Zealand Climate Standards (NZ CS)[1] are intended to explain an entity's journey to better manage climate-related risks and opportunities.

The vision of standard setter the External Reporting Board (XRB) is that New Zealand prospers through effective decision making for resource allocation informed by high-quality, trusted and integrated reporting. Good governance plays a critical role in this. Through this guide, the XRB, together with Chapter Zero NZ and the IoD, aims to support and enable directors to add value to their businesses and wider communities and prepare them to positively transform the businesses they govern for the future.

Transition planning helps to achieve this purpose. As stated by the Glasgow Financial Alliance for Net Zero (GFANZ):

This guide aims to support directors to understand, engage with, and guide the development of credible transition plans.

It outlines how to assess how climate mature the businesses are that you govern (see maturity scale page 28), and how you can approach long-term strategy informed by multiple scenarios (see page 18).

> “*Companies with credible transition plans may increasingly be able to access products and services tailored to low-carbon business models. In contrast, companies that do not have credible transition plans may face higher costs and/or restricted access to financial products and services (e.g., higher costs of capital) depending on the decision-making process of their financial institution(s).*[2]

1 Aotearoa New Zealand Climate Standards

2 Expectations for real-economy transition plans

Tē tōia, tē haumatia, kia rite, kia mau
Nothing can be achieved without a plan, workforce and a way of doing things. Be prepared to take action.

A transition plan is "an aspect of an entity's overall strategy that describes an entity's targets, including any interim targets, and actions for its transition towards a low-emissions, climate-resilient future" (NZ CS 1 – Climate-related Disclosures).

Transition planning: A director's "need to know"

Increasingly, climate change is causing significant systemic disruption. Its impacts are interconnected, deeply uncertain and unfold over a long-term horizon. While the transition to a low-carbon economy will require technological changes, it is not driven by technological readiness but by societal needs (i.e., reducing emissions), which differentiates it from any other major technological transitions of the past.

Disruptions will arise from physical and social forces. By contrast, corporate strategy is mostly driven and influenced by market forces (competition, technology, consumers, regulation and more). Climate change therefore requires different approaches and tools that many businesses may not be used to deploying on a day-to-day basis, such as scenario analysis.

Transition planning is not only a key part of climate-related disclosures, but a core element of robust business planning and a business's overall strategy. Undertaken in isolation, it can be an inefficient and ineffective exercise. To help prepare your business for a low-emissions, climate-resilient future, it should be integrated into your strategic planning process.

Transition planning asks the 'so what' question – *so what is your business going to do in response to what it has learnt from making climate-related disclosures?*

Businesses not subject to climate-related disclosures (CRD), should be asking themselves how they are considering climate-related risks and opportunities as part of their risk management and strategy processes.

Done well, transition planning can:

- Enable the board to govern and disclose the business's climate resilience
- Reduce your business's exposure to legal, trade and capital access risks, while highlighting market opportunities and improving attractiveness for investors/stakeholders
- Enable your business to identify and seize opportunities and business model changes, which will better ensure your business's success in the transition to a low-emissions, climate-resilient economy
- Enable the board to define a robust long-term strategic direction allowing for better decisions, avoiding lock-ins, and ensuring timeliness and right sizing of execution
- Improve your business's ability to navigate the increasing uncertainty of your operating environment, not just from climate change but from other disruptions
- Create confidence in, and support for, the case for change and transformation in your business
- Develop your business's capabilities, as it demands continuous dynamic and adaptive optioneering, planning and operationalisation

“To enable primary users to understand how climate change is currently impacting an entity and how it may do so in the future. This includes […] how an entity will position itself as the global and domestic economy transitions towards a low-emissions, climate-resilient future.”

(Strategy disclosure objective from NZ CS 1 Climate-related Disclosures)

What is transition planning?

Transition planning is the internal process to formulate, implement, monitor and adjust a strategy that will enable the business to operate, generate sustainable revenue, protect its assets and finance itself in a low-emissions, climate-resilient future.

Transition planning is about the repositioning and transformation of the business model and strategy in response to climate-related risks and opportunities. It involves exploring the options available, charting a pathway informed by the different risks and opportunities identified, and taking tangible actions. This is why a clear understanding of the business's purpose, goals and strategy is an important prerequisite.

While familiar strategic tools can be used, existing processes may need to be adapted to incorporate the implications of climate change as a systemic risk.

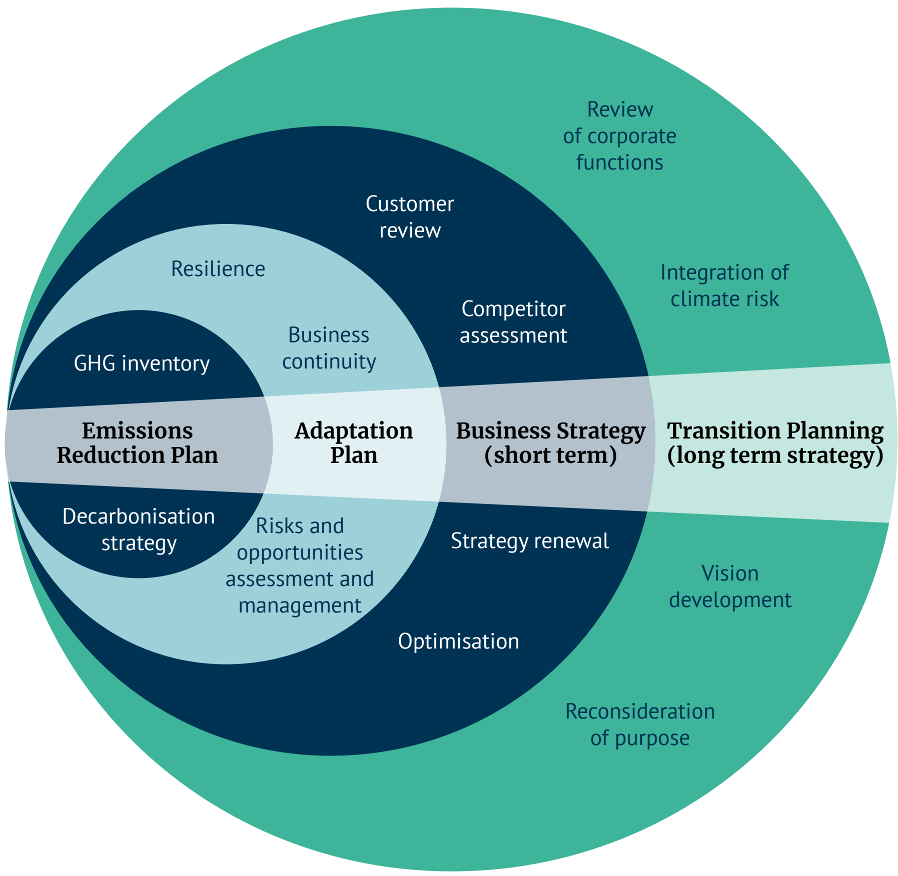
Your business has likely already completed elements of transition planning. Outputs from climate scenario analysis, emissions reduction plans, and adaptation plans can all be utilised when developing a transition plan (refer Figure 1).

Targets also play an important role in signalling commitment, enabling accountability and tracking progress. However, targets in disclosures should be used in support of a long-term strategic direction and a credible plan.

Once a strategy is (re)formulated, the business can develop its transition plan and chart a flexible pathway informed by the different risks and opportunities it has identified. The actions along this pathway will enable each business to build resilience to critical uncertainties, manage risks, and position itself to seize opportunities.

Figure 1: Climate change planning tools and processes

You have likely already completed elements useful to transition planning. Transition planning is building on previous work and bringing it into a consistent long-term repositioning and transformation strategy.



NZ CS transition planning

The ultimate aim of the NZ CS is to support the allocation of capital towards activities that are consistent with a transition to a low-emissions, climate-resilient future.

Many climate reporting entities (CREs) opted for Adoption Provision 3 in their first year, which exempts them from the full transition planning reporting requirement (see inset). However, CREs must still disclose what they are doing to prepare for transition planning.

While much of the transition planning process (see Appendix A) is 'behind the scenes', the objective of that process is to reposition and transform the business in response to what it has learnt about its climate-related risks and opportunities through its climate-related disclosures process (the "so what?").

The disclosure itself is what the business decides to share with its primary users to explain how its business model and strategy might change to address its climate-related risks and opportunities, and the extent to which its internal capital deployment and funding decision-making processes are aligned accordingly.

Transition planning has the potential to be a high-value process for all businesses. It is recognised that there may be short- or mid-term trade-offs (e.g., lower dividends, capital investment) required, so transparency is crucial for all stakeholders. It also forms a critical description of how businesses will position themselves as the global and domestic economy transitions towards a low-emissions, climate-resilient future. Further, it may signal that some businesses may become 'sunset' in nature, which is equally an important disclosure.

NZ CS 1 Climate-related Disclosures paragraph 16:

"An entity must include the following information when describing how it will position itself as the global and domestic economy transitions towards a low-emissions, climate-resilient future state (see paragraph 11(e)):

(a) a description of its current business model and strategy;

(b) the transition plan aspects of its strategy, including how its business model and strategy might change to address its climate-related risks and opportunities; and

(c) the extent to which transition plan aspects of its strategy are aligned with its internal capital deployment and funding decision-making processes."

Transition planning makes good business sense

In addition to disclosure requirements, transparency, stakeholder engagement, accountability and investor confidence, other reasons exist to engage with and undertake transition planning.

Trade

Currently 80 per cent of New Zealand exports by value go to markets that have mandatory environmental, social and governance (ESG) reporting either in place or proposed.[3] Global-facing companies, and businesses that are part of their value chain, are facing increasing expectations for transparency, emissions reporting and verifiable transition activities.

As climate-reporting regimes continue to expand globally – according to the Task Force on Climate-related Financial Disclosures, currently 60 per cent of world GDP is now subject to mandatory disclosures – there will be wide-ranging repercussions for New Zealand businesses. The global landscape of ESG reporting obligations, particularly in terms of climate and sustainability disclosure requirements and emerging trade measures that relate to climate change, is evolving quickly. Further, as the physical impacts of climate change strengthen and multiply, market expectations can change quite quickly.

The ability to trade internationally is increasingly reliant on you being able to understand your carbon footprint and being able to demonstrate you consider climate and other environmental impacts.

Opportunities ahead

Not everything we do (and are in the business of) has a future. But as the world changes, new needs will arise and businesses that align their value proposition accordingly are more likely to survive and thrive.

Every problem to solve is a business opportunity. Businesses that think in terms of 'value proposition', 'problem to solve' or 'jobs to be done',[4] will stay ahead.

For example:

- Battery makers are not actually in the battery market, but in the 'portable energy' market. Currently, batteries are a relevant option to provide portable energy for some uses. That might change in the future as technology progresses, as happened in the photography market when digital replaced film as a solution for recording photos.[5]
- A business that specialises in making steel products could see itself in several ways: as an expert in steel, competing with other materials, or as an expert in manufacturing solutions for the construction and industry sectors. Steel happens to be the most competitive option for many uses in construction and industry sectors today, but that might change in the future. If the business sees itself as a steel expert, then it could aim at promoting the use of steel, seek to procure low-emissions steel, and/or partner with businesses that have expertise in other materials to leverage the unique property of steel while staying relevant. Alternatively, it could diversify into other materials to maintain relevance in its core markets.

Linking the problems that a business is currently trying to solve to the climate scenarios it has developed provides a useful framework: these problems might be much less of a priority or even irrelevant for customers in some scenarios. Conversely, new problems that the business may be well-placed to solve could become much more important to these customers (or new ones) in the future.

Moreover, disclosing your transition planning is an opportunity for a business to own its own narrative. Transition planning is an opportunity to articulate the connection between climate-related risks and opportunities to strategic priorities, capital allocation, metrics and targets.

Some businesses with sunsetting activities could choose to adopt a winding-down strategy, maximising current returns without making further investment decisions that may not be aligned with a climate-changed world. Being transparent will be important so investors' decisions can be made accordingly.

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3 Protecting New Zealand's competitive advantage

4 What is the jobs to be done framework (JTBD)?

5 Innovation and the transition to a low-carbon future

Access to capital and market value

The pace and scale of the transition will vary between sectors. Regardless of the sector, the degree of credible action on climate change is under increasing scrutiny. With an increasing emphasis on responsible investing and lending, access to capital can be impacted.

Evidence shows that businesses that proactively respond to climate risk are rewarded by the market: those that don't are punished.[6] Conversely, prioritisation of sustainable activities to support climate transition can increase access to capital and diversity of investors.

The Responsible Investment Association Australasia's 2024 *Voice of Aotearoa* report found that retail investor demand is growing and maturing:

- 77 per cent of respondents expect investments to be ethical or responsible
- 57 per cent would move their investments if they did not align with their values
- Investors wanted to avoid investments that cause environmental damage (89 per cent), power generation using fossil fuels (72 per cent) and fossil fuel production (71 per cent)

Similarly, PwC's *Global Investor Survey 2023*[7] found that 89 per cent of investors wanted companies to disclose the environmental and social impacts of their investments, increasing from 60 per cent in 2022.

In New Zealand, major banks have CRD obligations including disclosure of their scope 3 'financed emissions', which are the emissions of their customers. Banks are increasingly required to consider and manage the climate-related risks and opportunities associated with their lending practices.

A credible transition plan presents a unique opportunity for a business to unlock the funding it needs to transition toward new value propositions.

Liability

There is increasing scrutiny of the gap between high-level ambitions and targets, and plans to achieve those targets, including capital allocation. Bridging that "say-do", or strategy-action gap via transition planning is a key way to manage the potential for greenwashing, liability risk, and retain stakeholder trust and confidence.

Climate lawsuits are increasingly used to push for more decisive action to slow climate change. Successful climate lawsuits against some governments have also resulted in new regulations (see Figure 2).[8]

New Zealand was ranked seventh in the list of jurisdictions with the highest number of cumulative climate change litigation cases, according to the 2023 United Nations Environment Programme Global Climate Litigation Report (see Figure 3).[9]

For directors, liability for forward-looking statements is a valid concern and globally, is resulting in increasing levels of greenhushing. New artificial intelligence tools trained on climate science text, like the IPCC reports, are now able to analyse large amounts of information and provide indicators such as the 'cheap talk index',[10] which assess the level of credibility and commitment of climate claims.

For many topics, relying on data is the go-to solution. However, when a business faces making long-term decisions on matters with significant uncertainty, there is a risk of decision paralysis and inaction. The challenge is not new – and it can be alleviated by employing the precautionary approach or principle.[11]

The precautionary principle is contained within many international instruments, and advocates for precaution when scientific evidence about an environmental or human health hazard is uncertain, and the stakes are high. In practice, this means directors can focus on being explicit about what is knowable at the time of their decision.

Documenting your assumptions is especially important for topics such as climate, where there is a growing gap between what decision makers would like (i.e., hard granular data) and what science can realistically provide. Nonetheless, scientific evidence is providing key insights that should be acted upon.

For example, scientists had predicted there would be a global pandemic many years before Covid-19. They expected it would come from a coronavirus, would transmit from animals to humans, and predicted how fast it would spread in our globalised world. But they couldn't say when, how much, or for how long. The businesses and countries who took no actions due to lack of specifics were caught unprepared.

6 Corporate climate risk: Measurements and responses
7 PWCs global investor survey 2023: Insights for New Zealand
8 Global trends in climate change litigation: 2024 snapshot
9 Global climate litigation report: 2023 status review
10 How cheap talk in climate disclosures relates to climate initiatives, corporate emissions, and reputation risk
11 The Precautionary Principle

Figure 2: Number of climate litigation cases within and outside the US, 1986-2023

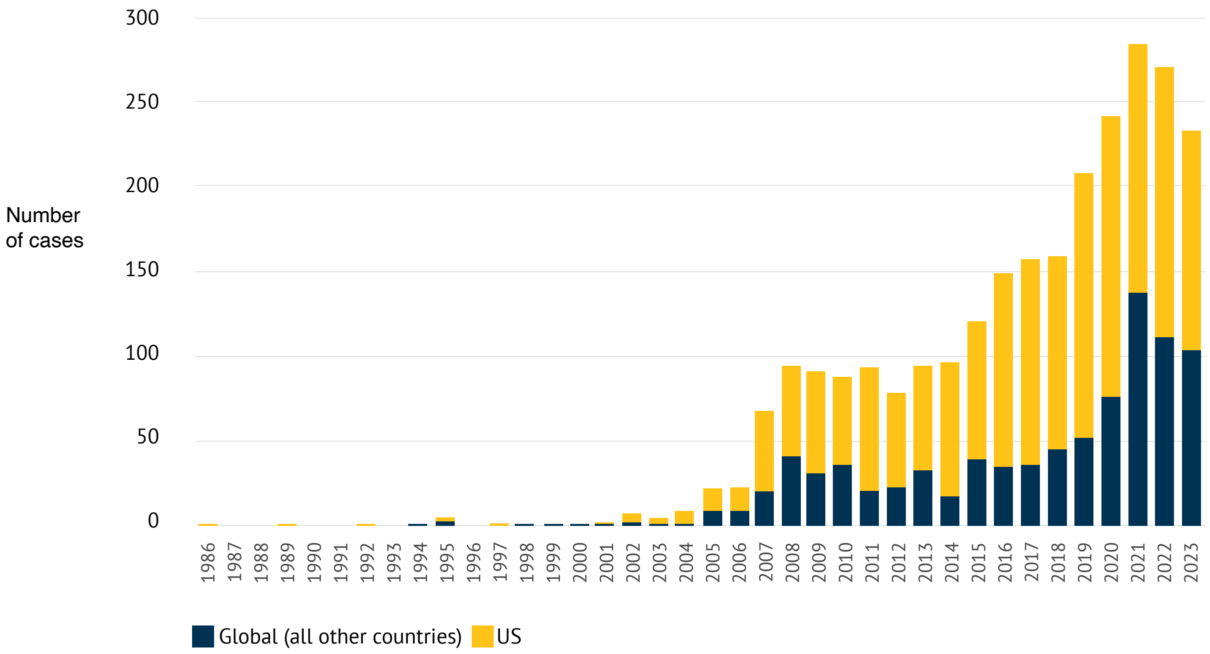
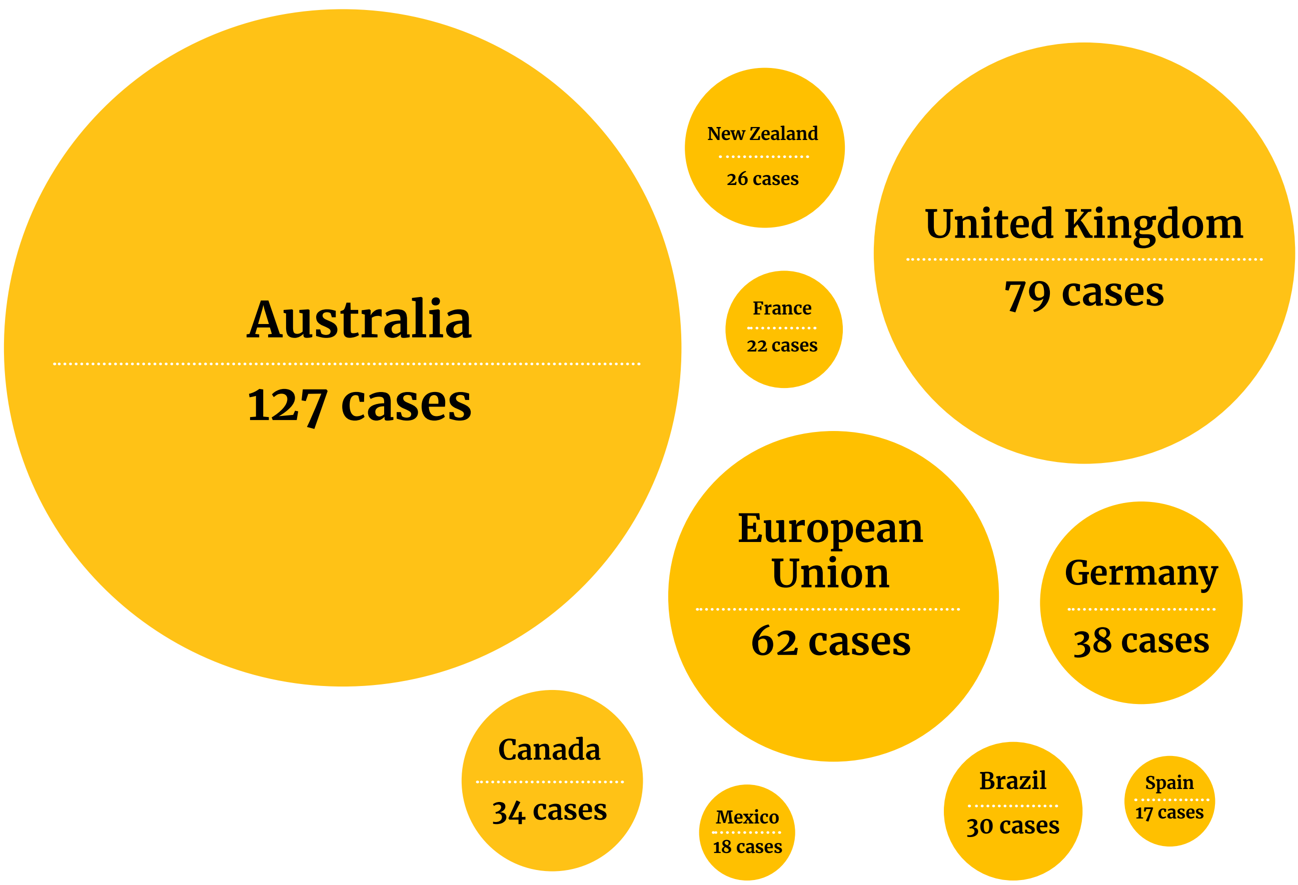


Figure 3: Top 10 jurisdictions wih the highest number of cumulative cases



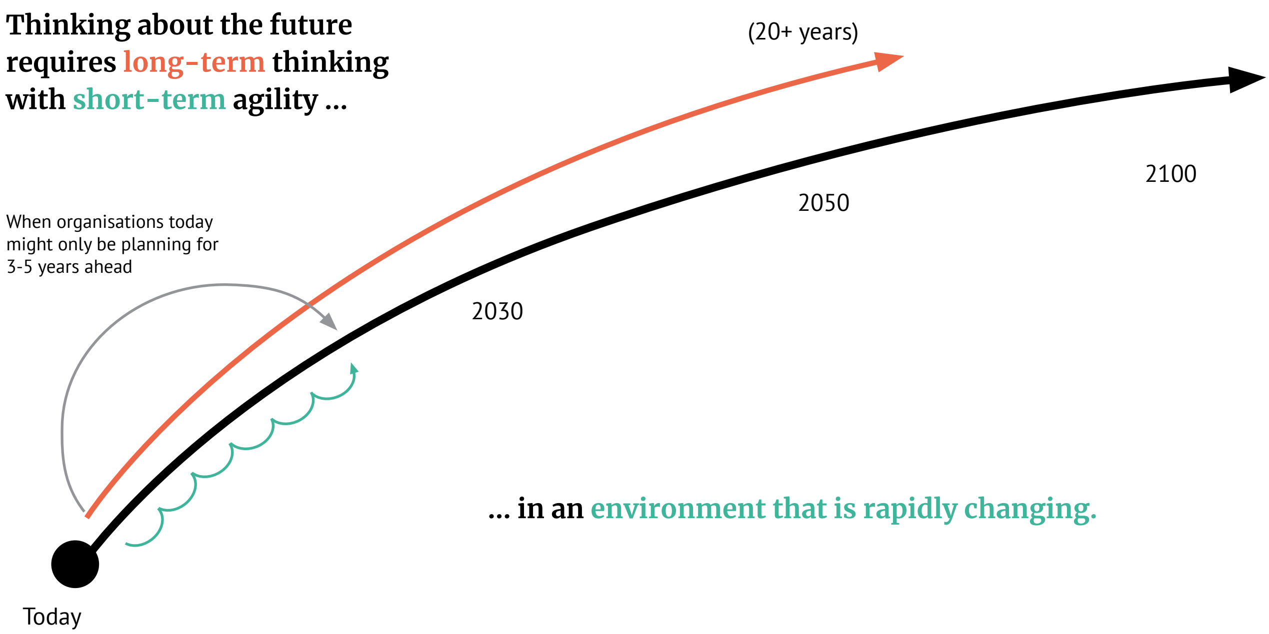
The role of directors in transition planning

Climate-related disclosures and transition planning are important elements of the board's oversight as this includes evaluating and adapting the business model and strategy to achieve emissions targets, address risk, and seize opportunities for the transition towards a low-emissions, climate-resilient future.

Appropriate leadership from the board ensures that a business's culture, structure and strategy are strongly aligned and support innovation and adaptation. An innovative business will challenge established approaches, constructively assess failures and adjust strategies as new insights emerge. The board needs to give the business mandate to invest, whether that is investment is in low-emissions assets or building internal capability, and/or capacity for new business models.

An agile board is needed (see Figure 4). The board must accept that, in balancing short-term pressures with the long-term interests of the business, tomorrow's answers will likely be different from today's. There are many uncertainties about the future, but there is also a lot that is known. Directors need to be curious and not use uncertainty as a reason to delay action. Thinking about the future requires ongoing questioning of assumptions and a continuous learning mindset.

Figure 4: Long-term thinking with short-term agility



How to get started as a director?

Transition planning impacts across the entire organisation and the future direction of the business. Directors have a critical leadership and oversight role to play in transition planning.

- Develop your own competencies, knowledge, and expertise
- Revise the board or committee structure/reporting lines to ensure climate change/transition are embedded in your strategy and decision making
- Ensure the business is sufficiently supported, resourced and incentivised
- Engage with the transition planning process challenging the robustness and depth of the thinking and helping balance the short-term pressures with the long-term interests of the company
- Provide board oversight of integrating and operationalising transition planning
- Set, review and adjust risk appetite in a clear and actionable way
- Ensure interim targets and actions are in alignment with the strategic ambition, and with defined roles and responsibilities
- Ask for frequent insights, briefings and deep-dives into new transition-related developments
- Seek to understand and engage with shareholders and stakeholders
- Support investors and your business to make informed capital allocation decisions
- Check that the assumptions underlying the business's purpose and strategy have been considered and stress-tested in the climate scenarios

Long-term strategy

Reviewing the strategic direction of your business while facing deep uncertainties is challenging. Best practice guidance states that the strategy should be co-developed by the board and management, but that the board has a lead role in outlining a vision, defining values and setting goals.

Co-designing your long-term strategy with management

As guardians of the organisation's purpose and long-term sustainability, directors have ownership of the long-term strategy, while management can focus on shorter-term business goals and objectives that progress the organisation towards the long-term direction set by the board.

It is important for directors to keep two key considerations front of mind when developing a strategy that will be impacted by systemic risks like climate change.

A) **Strategic foresight:** Navigating high uncertainty requires taking a longer-term view, not a shorter one.

B) **Foundational assumptions:** Are the services or conditions, mostly outside of a business's control, on which the business relies to exist, operate and generate sustainable revenue, as relatively stable as they have been over the past few decades?

Strategic foresight

By using foresight to identify a direction of travel, directors will enable management and the rest of the business to plan accordingly. This will allow better decisions, avoiding lock-ins, and ensuring timeliness and right sizing of execution. Management will be in a better position to devise a shorter-term business strategy that is nimble yet aligned with the long-term strategy.

Directors could constructively challenge management to take a longer-term view by asking:

- How could we meet our customers' needs without GHG emissions?
- What new needs would our customers have in each of our climate scenarios? How could we deliver solutions?
- Which new needs would we be well placed to meet in each of our climate scenarios?

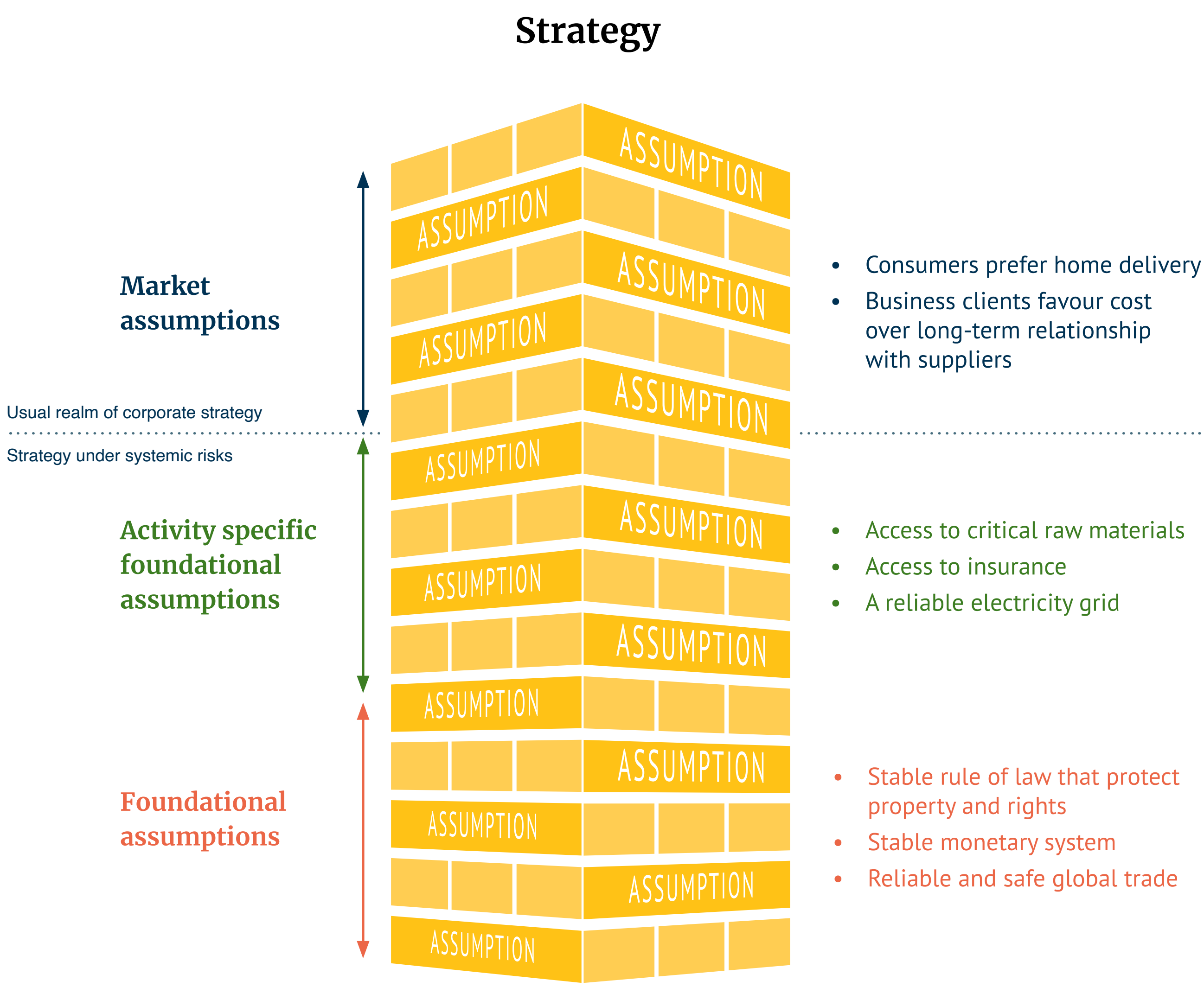
Foundational assumptions

What can distinguish a good strategy from a bad strategy is the quality of the assumptions upon which it is built (see Figure 5). Corporate strategy tends to focus on market forces such as competition, technology, consumers and regulation. However, systemic risks throw into question the subset of foundational assumptions that are often taken as an unchallenged basis of the operating environment.[12]

Foundational assumptions underpin and support market and strategic assumptions. Directors should ensure that all key assumptions are systematically identified, properly challenged and regularly reviewed as part of climate scenario analysis and transition planning exercises.

[12] For more information on key scenario assumptions, inputs and data needs see the Chapter Zero New Zealand guide Effective climate governance – climate scenario analysis.

Figure 5: Foundational assumptions as building blocks of corporate strategy



Developing a strategy informed by multiple scenarios

Setting clear and concrete strategic direction when facing deep uncertainties is challenging. While businesses might be used to demonstrating some tactical flexibility to adjust to shifting markets, the idea of multiple possible strategic directions at once can be unsettling.

Linking with scenario analysis

In practice, for a given business, the best value proposition in a fast-transitioning world (e.g., in a 1.5°C scenario) will rarely be the same as that in a world exposed to above 3°C of global warming. Beyond the differences in terms of physical impacts, the operational environment of the business will be very different in both potential future states of the world. Plus, the future will never play out exactly as set out in any given scenario.

Waiting until uncertainties decrease is unlikely to be a viable option. By the time climate-related uncertainties are resolved, a business might be locked out of its best strategic opportunities and have locked in liabilities such as stranded assets.

The goal for most businesses will be to define enough strategic direction to enable action, while keeping its options open, and pre-positioning itself to pursue its opportunities and manage its risks across the range of potential outcomes explored in its scenarios.

To do this, businesses can explore what the business's long-term value proposition(s) could be in the different possible worlds, as this will provide insights to express its strategic intent.

This means exploring the questions:

1. What would the business's value proposition(s) be in each of these potential worlds?
2. What might the business ideally look like under each of these scenarios by 2050?

Figure 6 illustrates this envisioning exercise. A business imagines its most desirable value proposition(s) in different possible operational environments in several, very different, potential future worlds, based on the insights it has. This will, in turn, inform what the business would need to become to be successful in each of these different future worlds, and the gap to bridge compared to the current situation.

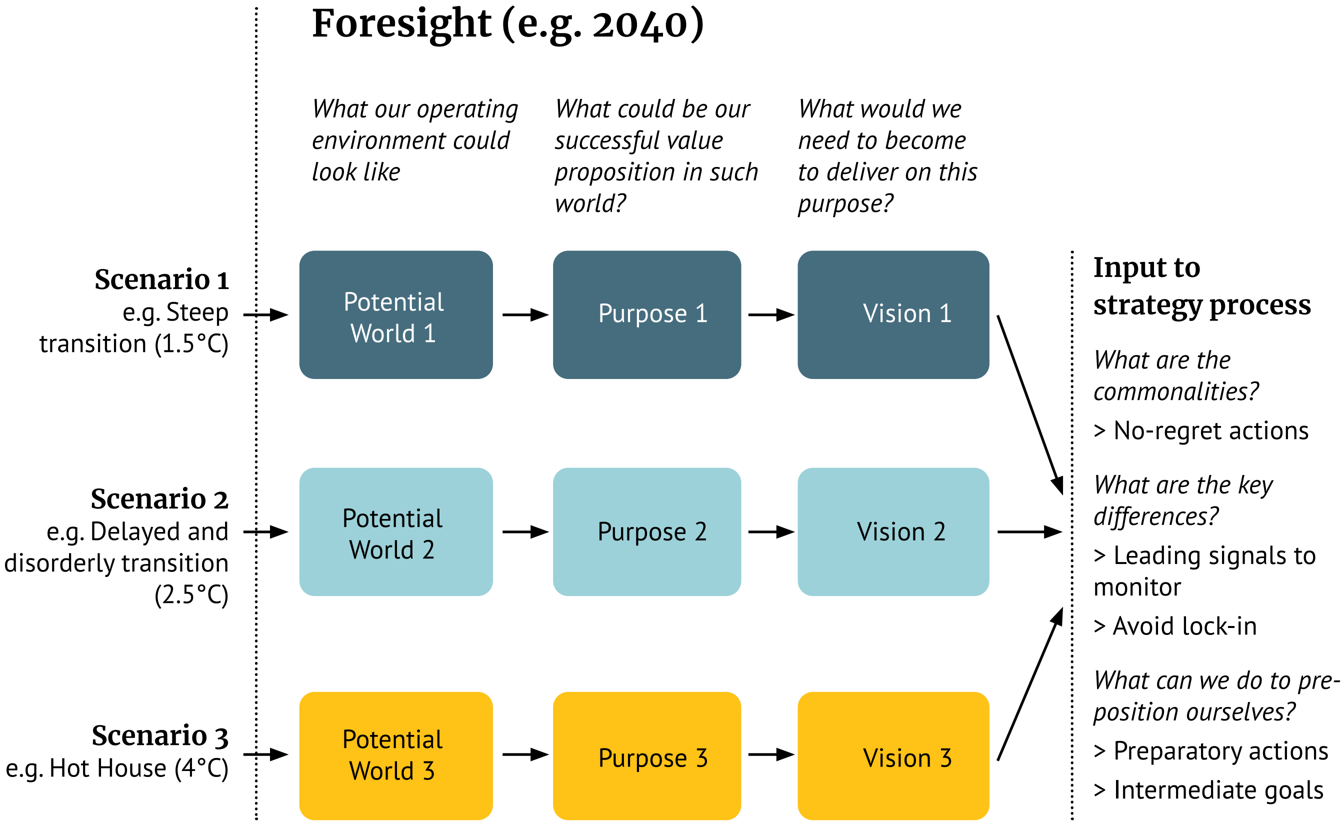
Narrative exercises describing how the business successfully thrived under each of the scenarios (i.e., 'success stories') can enrich the strategic thinking and refine the vision for the business.

While the future cannot be predicted, identifying the key commonalities and differences between the success stories of different scenarios can provide useful insights. Commonalities can provide confidence in making some decisions subject to fewer uncertainties.

Key differences between the scenarios can inform a business of what it needs to monitor and what preparatory work might be useful. For example:

- A business anticipating that a product it provides would be either surpassed by very low-emissions alternatives in a quickly transitioning world, or would face much lower demand in a warming world, might decide to stop its investments in this product as a consequence, and opt for an extraction or divestment strategy for its related assets.
- A business envisioning radically different markets for its products from one scenario to another might seek to identify leading signals to monitor how the related uncertainties trend. It might also seek to pre-position itself for opportunities by doing research or pilot projects. Such preparatory work shortens lead time to seize opportunities, which enables later decision making and thus reduces risks.

Figure 6: Linking strategy with scenario analysis



Guiding this process

Directors need to consider how uncertainty will be managed over the long term, what tangible actions could be taken now, and what quality controls are in place.

Managing uncertainty:

- What are the potential options available to manage critical uncertainties in an adaptive strategy? How will these potential options be identified?
- Which signals and trigger(s) will be monitored to inform future decisions?
- Which preparatory actions will be taken to put the entity in the best position as part of its adaptive strategy?

Tangible actions:

- Which short-term actions can help the business achieve a better strategic position and build resilience?
- When will these actions take place, and how much resource will be dedicated to them?
- Where are resources going to come from to support these actions? Is it sustainable? Are new operating models required?

Quality controls:

- Actions from the business are better than dependencies on others' actions.
- Emissions reduction is only one part of the story and doesn't address the whole range of climate-related risks and opportunities.
- Beware of tunnel vision: the interactions and dependencies the entity has with the broader systems it operates in are critical considerations. Assuming all else will remain equal is implausible.

“While no entity can predict the path to 2050, frequently updated transition plans make pledges concrete while highlighting uncertainties, assumptions and barriers.”

Integrity matters: Net zero commitments by businesses, financial institutions, cities and regions, United Nations’ High-Level Expert Group on the Net Zero Emissions Commitments of Non-State Entities, 2023

Transition planning with the IoD's Four Pillars of Governance Best Practice

Determining purpose

The direct and indirect impacts of climate change ultimately threaten the long-term viability of almost every business, so how we do business should reflect this. Directors need to understand, address and communicate the impacts of climate change and their business's ability to transition and create value.

Climate change will not be experienced as one shock but a multitude of cascading impacts of increasing strength and frequency.[13] Rather than treating climate change as an emerging side topic, it should be a core part of the board's focus, embedded in a business's strategy, and understood and integrated across its whole operating model.

Transition planning determines how the business will achieve its purpose, goals and strategy:

- Through the significant disruption of transition to a low-emissions climate-resilient economy
- While the physical effects of climate change are continually increasing in severity and frequency, triggering in turn
- Shifts in market forces such as customers' ability to pay, competitors' behaviours, or supply chain costs and reliability

Along with your business's purpose, goals and strategy, the key inputs to transition planning are your:

- Climate scenarios (and the assumptions and material drivers that underpin them)
- Climate-related risks and opportunities
- Your current understanding of emissions and climate-related risks posed by, or inherent in, your value chain

Strategy without foresight makes companies vulnerable to outside disruptions. Foresight without strategy renders scenarios unactionable. Each on its own has value, but the current operating environment requires both. When strategy isn't performing its intended job, businesses cannot continually improve, leverage disruptive technologies, nor adapt to new market conditions.

A good forward-looking strategy process requires minimal adaptation to consider new parameters such as climate (or nature or arificial intelligence) and will enable the use of existing resources, experience, and capabilities to support the business's transition planning.

A disciplined and systematic approach to strategic foresight will help ensure your business is resilient in the face of unforeseen disruption. Only focussing on familiar threats and known risks can lead to businesses being caught unprepared and having to react under duress.

Pillar 1: Determining purpose

The board adds value by leading the development of the entity's purpose, goals and strategy. The board must take ownership of the entity's strategic direction. Long-term business sustainability is a critical focus for the board.

IoD, Four Pillars 2021

[13] Climate change risk assessment 2021

An effective governance culture

An effective boardroom culture is fundamental to operating as a value-adding board. Boards have a key role in setting the tone for organisational culture and ensuring that it aligns with, reinforces and gives life to its strategy and purpose. Together, culture, purpose and strategy are the essential elements of what a business does and why.

As a strategic response to disruption, transition planning will likely require organisational and process change, and there will need to be an increased capacity for flexibility and innovation. The board has a key role in establishing and leading this culture and mandating this change. How this is to be achieved, and the governance boundaries and delegations needed to provide assurance to the board should be discussed, agreed and regularly reviewed.

Transition planning is an ongoing process and needs to reflect the latest understanding of material climate-related risks and opportunities. It is a living 'document' which will continue to evolve and requires regular governance oversight. While there isn't a hard and fast rule on the frequency of review, since most businesses are just starting their journey in adjusting to a climate changing world, each year will bring progress and there is an expectation that primary users will be informed of any material progress in a timely manner (see NZ CS 3 General Requirements for Climate-related Disclosures).

A business's strategic planning cycle may need to be adjusted to accommodate the frequency of review.

- Expect board papers (on any topic) to clearly reflect consideration of and integration with, the business's current transition plan
- Ensure that climate scenarios become an integral part of your consideration of climate risk and strategic planning
- Consider what the accelerating, and long-tail nature, of climate risk means for your risk appetite and governance

Businesses taking a strategic, long-term view, investing today in their human capital, developing their future value proposition and starting the 'no-regrets'[14] work now, will be better positioned to adapt to evolving trends, seize opportunities and protect market access.

Pillar 2: An effective governance culture

The board adds value by acting as a team with a high-performance culture committed to engaged, quality governance of the entity. It supports open debate, diversity, thoughtful challenge and constructive dissent. Directors lead through high standards of ethical behaviour, commitment, candour, and integrity. This culture is characterised by effective relationships between directors and with management, shareholders and stakeholders.

IoD, Four Pillars 2021

[14] This is shorthand for 1) the actions that will improve an entity's position in any scenario; and 2) actions where the upsides in a certain scenario are greater than the downsides (e.g. a small investment that can easily be scaled-up or down). Conversely, beware of what appears 'no-regret' today but could limit your options tomorrow. It is important to contextualise short-term decisions with long-term goals as this allow an entity to be opportunistic and avoid wasting resources on projects that are not aligned with the long-term plan.

Holding to account

The role of the board is to clearly articulate what the executive and management team must deliver, through the operating model, and then actively support and appropriately resource any people, systems or process changes required for this. Where the changes identified are beyond the immediate capacity or capability of the business or available technologies, the board needs to consider what resourcing is required and the risks of either inaction or staged action.

While governance is frequently described as being 'hands off', there is an increasing argument for collaboration and knowledge-sharing between the board and management.

In the transition planning process, directors should ensure that the assumptions underlying the business's purpose and strategy are considered and stress-tested in the climate scenarios to inform the strategy's resilience to the critical uncertainties identified. Asking a lot of probing questions ("what about…?", "what if…?") to stress test the robustness and depth of the thinking is key.

The board should receive regular reports and assurance from management on the climate transition-related changes being implemented, progress against agreed milestones, targets and goals, and/or actions taken to reduce risks. Goals and targets should be reviewed and reset as needed to ensure they remain relevant and achievable. Boards need to ensure additional briefings are occurring as needed to continue to develop an understanding of new technologies, products or services that are being considered.

The operating environment for businesses is increasingly challenging and complex. Businesses are facing ongoing volatility, uncertainty and ambiguity. Instead of planning cycles being further out, they're shrinking down to the next couple of quarters, while at the same time long-term thinking is required.

Climate change, nature and technology mega-trends are reshaping the operating environment at an increasing pace. Waiting for uncertainties to disappear is not a winning strategy. Deep uncertainty merits deep questions, curiosity, thoughtful challenge and even constructive dissent.

Pillar 3: Holding to account

A value-adding board holds management to account through informed, astute, effective and independent oversight of performance and conformance matters. It does not do the job of management but ensures purpose and strategy are understood by management and implemented. The board sets the risk appetite of the entity and oversees and monitors risk management.

IoD, Four Pillars 2021

> “ *The scale of the challenge climate change poses to organisations and operating environments justifies directors coming down to coach from the sidelines.*
>
> *What difference can directors make, KPMG & Chapter Zero NZ, 2023*

Effective compliance

Through its systemic nature, climate change will impact the whole operating environment, and therefore presents material financial and systemic risks to all businesses. Good climate governance is about building long-term resilience and value.

While directors must comply with their duties and responsibilities, climate change and transition planning are more than a regulatory responsibility. Lenders, investors, insurers, stakeholders and more are increasingly demanding disclosure and understanding about the nature of businesses' climate risk and what mitigation and transition planning is in place to respond to it. This is expected to continue as more countries adopt reporting provisions and financial institutions increasingly focus on climate engagement.

For CREs directors are responsible for ensuring that their climate-related disclosures follow the requirements of NZ CS 1 Climate-related Disclosures and NZ CS 3 General Requirements for Climate-related Disclosures, explaining how the business will position itself as the global and domestic economy transitions. This includes how business's models and strategies might evolve to address climate-related risks and opportunities, and the extent to which transition plans are aligned with internal capital deployment and funding decision-making processes.

For example, dialling down communication on environmental claims might provide some immediate relief from the risk of inadvertently making misleading claims based on imperfect knowledge, but is at odds with investors' and stakeholders' expectations of transparency, and can erode trust.

A more balanced approach is to acknowledge that nobody has the perfect plan, and that adaptability is a defining characteristic of an effective transition plan. There can be equal, if not greater, risk in not disclosing a transition plan because it's 'not ready' or 'might change', than in putting out a plan acknowledging its assumptions, gaps and dependencies and that it is likely to change as transition unfolds.

Climate change is a systemic risk. This means that it is relevant to a director's duty of care for all businesses. No business operates in isolation and will always have dependencies on its supply chain. Everything and everyone will be impacted, directly or indirectly, to varying degrees.

There are deep uncertainties, but the consequences of continuing business-as-usual isn't one of them - and ignoring what is known and foreseeable is a breach of fiduciary duties.[15]

As scrutiny increases and expectations grow louder, focusing on the underlying long-term work is the best way to protect your business, and yourself, from these risks.

Pillar 4: Effective compliance

The board adds value by ensuring the entity is, and remains, solvent. It ensures the probity of financial reports and processes, and a high standard of compliance with regulatory environments. Directors must comply with their duties and responsibilities in relation to the entity, its shareholders and other stakeholders. Excellence in governance is enhanced through complying with the spirit as well as the letter of the law.

IoD, Four Pillars 2021

> “
>
> *Directors' duties of due care and diligence require them to think through climate-related risks and opportunities as part of taking a long-term perspective, in the decision-making process of the business.*
>
> *Primer on climate change: Directors' duties and disclosure obligations, Climate Governance Initiative, 2023*

15 Directors' duties navigator: Climate risk and sustainability disclosures 2024

Considerations for directors

A fundamental shift in business and finance is required to address the challenge of climate change and the need to transition to a low-emissions, climate-resilient economy.

Transition planning, and the disclosure of transition plans, are designed to support the transformation of the business model and strategy in response to climate-related risks and opportunities. Directors have a critical role in adjusting strategies to reposition their businesses to address risks, seize opportunities, unlock value, and build resilience and stakeholder confidence.

- Do you understand your organisation and industry long-term risks and opportunities?
- Do the board and management have the tools and resources to lead your strategy review and repositioning?
- Have you engaged with your supply chain, investors, lenders, employees and key stakeholders?
- Are you collaborating across the sector?
- Have you developed challenging climate-related scenarios?
- Are you receiving regular updates to your board on climate and nature-related impacts, risks and opportunities and progress towards your climate and sustainability targets?
- How are you using the climate-related disclosures framework as an opportunity to transform your business model and strategy?
- Have you assessed the level of climate and sustainability knowledge within the board and across the business and developed plans to upskill?
- Are you setting the culture from the top to support embedding of climate and sustainability and business-wide transformation?

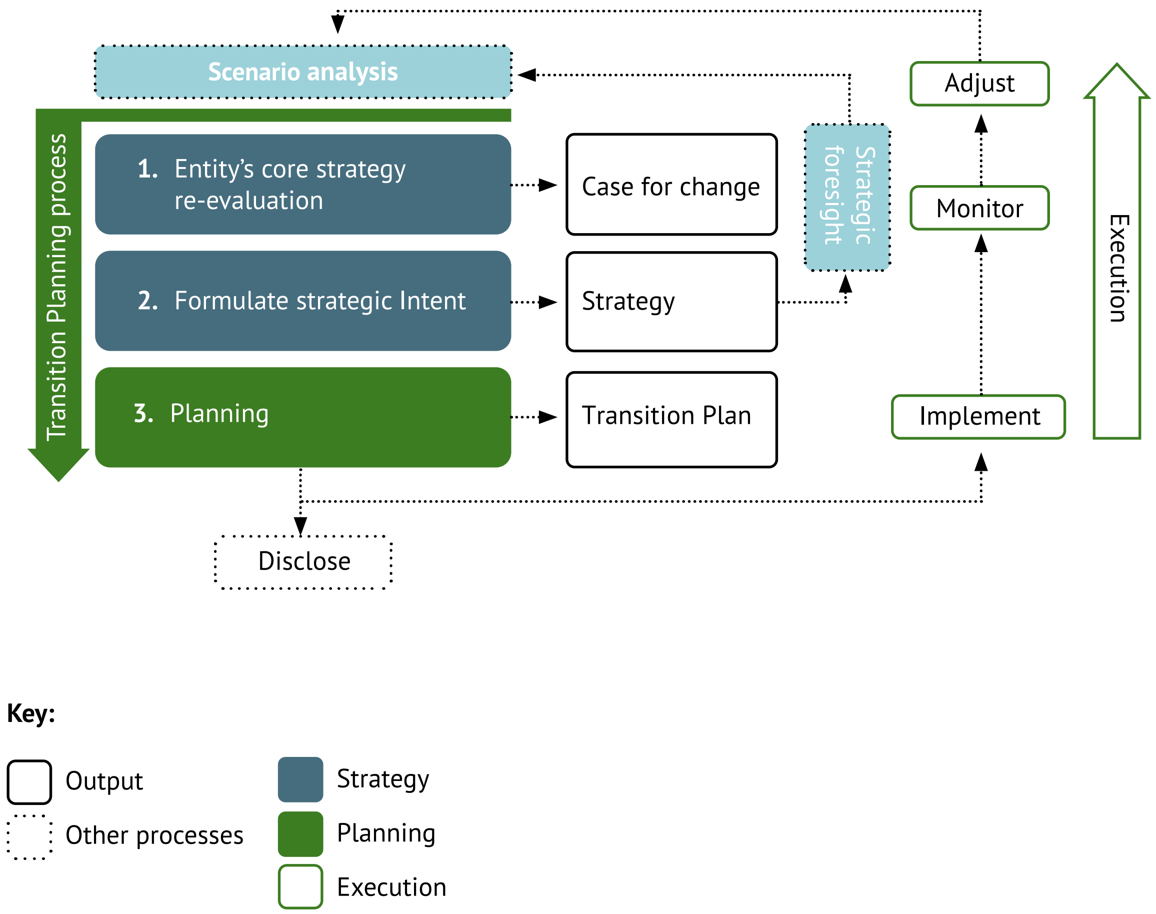
Resources

Standards:	Aotearoa New Zealand Climate Standards
	Scenario analysis and climate-related disclosures
Resources:	XRB staff guidance: transition planning
	The TPT disclosure framework
	Chapter Zero Transition Planning Toolkit
	What difference can directors make?
	Effective climate governance - climate scenario analysis
	Effective climate governance - board structure and capability
Articles:	Climate transition plans under the spotlight
	Transition planning: a global outlook for board directors
	Climate transition plans: CEOs on how to deliver more than just net-zero

Appendix A.
Transition planning process and roles

Transition planning process

This illustrates the three main steps of the transition planning process, each with their expected output, and how it fits into a strategy-execution loop. The main difference with existing strategic planning processes are the longer time frames and the need to take a systemic view. As a result, it can highlight blind spots in existing processes and shorter term strategic planning ('Case for change'), creating the need for an adaptive strategy able to better manage systemic uncertainties ('Strategy'), and more adequate planning to better position the organisation in a volatile, uncertain, complex and ambiguous (VUCA) world.



Transition planning roles

Provided below is a general outline of what would be expected from each role within the organisation, at each step of the transition planning process.

Roles matrix by function	**Sustainability Officer** (SO)	**Support functions** (finance, risk, strategy...)	**Management**	**Directors**
Entity's core strategy re-evaluation	Enrols and coordinates others across the organisation to build the business case for change	Support SO in building the case for change		Approve the case for change
Formulate strategic intent	Support	Support	Co-develop the strategic intent	Co-develop and approve the strategic intent
Planning	Coordinate	Support	Accountable for the development of the transition plan	Approve the transition plan

Appendix B.
How climate mature is your business?

Climate readiness/maturity scale - our progress

	LOW	MEDIUM	ADVANCED
	Compliance To meet NZ CS / auditor recommendation	**Risk mitigation** Managing risk and/or response to stakeholder expectations	**Strategy** Transition planning is a strategic imperative for our business
Pillar 4 – Effective compliance	**Internal focus** We have explored alternative climate scenarios and have not identified any material risks or opportunities	**Self-awareness** We have identified and mapped strategic drivers and are monitoring for early signals of change	**System awareness** We have operationalised adaptive planning and responsiveness to improve our resilience to climate-related disruption across our value chain
Pillar 1 – Determining purpose	**In development** There are different views among senior leadership on the materiality of climate change impacts for the business	**Shared situational awareness** We have a shared understanding of our operational strengths, weaknesses, opportunities and threats in each of our climate scenarios	**A clear strategic case** We have a shared situational awareness and have mapped our sector and have a view of how key stakeholders might react in each climate scenario
	Short-term focus We have added climate change at an operational level, but it is yet to be connected to the core business strategy	**Exploration of long-term strategic options** We have explored and assessed our potential options for our value proposition to stay relevant and viable. It hasn't translated into a shared strategic intent yet	**Strategic transformation** The board and management share a long-term vision including clarity and agreement on long-term potential objectives, no-regrets options, strategies to adopt, and critical uncertainties to monitor
	Aspirational targets We have ambitions or aspirational targets but have not started detailed transition planning	**Planning underway** Our strategic intent is understood and has buy-in from throughout the business and work is underway to progress and finalise our transition plan	**Transition plan adopted** We have a clear transition plan with key milestones, risks and opportunities positioned along a timeline with signals to monitor, preparatory actions, and potential pathways laid-out to inform our decisions

Climate readiness/maturity scale - enabling factors

(From strategy and plan to successful change)

	LOW	MEDIUM	ADVANCED
Pillar 2 – An effective governance culture	**Mostly delegated** Climate-related matters are mostly discussed and addressed at the committee level	**Standing item on Board's agenda** Climate-related matters are discussed and addressed at the board level, with a board member or committee tasked to stay across it	**Embedded** Our whole board has embedded climate throughout all aspects of our decision-making and operating environment
	Reactive Our business is lean and focused on operational optimisation. Change tends to be perceived as a threat	**Fit and nimble** We lead from the top implementing a change management programme and foster open communications throughout the business to embed the transition plan into the business culture and practices	**Innovative and resilient** Our board and management walk the talk and model adaptability. Our employees are empowered, and cross-functional collaboration is actively encouraged and enabled. Trust, continuous improvement and innovation are by-products of our business culture and structure
	Trusted advisors We have some climate or sustainability expertise to inform management and governance but not integrated across the business	**Shared awareness** Every level of the business has a clear understanding of the challenges and opportunities that climate raises for us and is able to actively contribute to our resilience	**Collective responsibility** We have the expertise required across the organisation to support the business in what it is transitioning into
Pillar 3 – Holding to account	**Climate is in our risk register** Climate-related risks are managed the same way as other risks, with a focus on risks relating to the physical impacts of climate change	**Climate is a key strategic risk** Climate change is recognised as a systemic financial and strategic risk that we identify, monitor and manage. Our risk management system is tailored for the specificities of climate risk (physical and transition), and climate-related risks and opportunities are a key input of our strategy	**External risks and cascading impacts integrated** Our risk function has the capability and processes designed to manage external, uncontrollable risks including the cascading effects and risks interactions of climate change
	Case-by-case We allocate funding to climate-related initiatives on an individual business case basis	**Climate screening** Our main resource attribution decisions include screening regarding our climate-related objectives	**Integrated** All significant investments are part of our long-term transition planning strategy

About Chapter Zero New Zealand

The Institute of Directors New Zealand (IoD) is proud to be the host of Chapter Zero New Zealand, the national chapter of the Climate Governance Initiative (CGI). This global network seeks to mobilise, educate and equip directors with the skills and knowledge necessary to address climate change at the board level.

Chapter Zero NZ is grateful for the support of our key partners who provide guidance and expertise to help us serve the director community.

Chapter Zero New Zealand
The Directors' Climate Forum

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