TCI Fund Management Limited

Ray McDaniel
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Dear Ray,

Carbon Emissions Disclosure

TCI Fund Management Limited manages over $30 billion across a range of asset classes. Since inception of the business over 15 years ago, cumulative investment returns have substantially outperformed equity index benchmarks.

TCI is a major shareholder in Moody's with a 3% holding.

Investment approach and engagement

As part of our investment process we assess a range of ESG factors, particularly climate change risk.

TCI believes that climate change-related risks, in particular a company's greenhouse gas (GHG) emissions, will have a material effect on a company's long-term profitability, sustainability and investor returns. These risks include regulation, taxation, competitive disadvantage, brand impairment, financing, physical asset impairment and litigation.

We actively engage on ESG to help us understand, quantify and influence a company's exposure to climate change-related risks and the way it is managing those risks.

Emissions disclosure

We require companies in which we invest to make appropriate and timely public disclosure of carbon and other GHG emissions. Such disclosure should include targets for emissions intensity reduction and absolute level reduction.

TCI fully supports compulsory disclosure on a standardised basis and the use of the Task Force on Climate–related Financial Disclosure (TCFD) reporting framework (www.tcfdhub.org).

In our view, reporting to CDP (www.CDP.net) is the best way to implement TCFD. **We expect all our portfolio companies to make full annual public disclosure to CDP.**

Low-carbon transition plans

We expect companies in which we invest to have a credible, publicly-disclosed plan to reduce GHG emissions. This plan should include measurable science-based targets that align with the Paris Agreement, which requires full de-carbonisation of economies (net zero emissions) by 2050.

Actions that should be included in a low-carbon transition plan are to:

1. Change business processes to reduce the company's carbon footprint;
2. Introduce efficient energy management into buildings and factories;
3. Source low carbon energy through direct generation or power purchase agreements;
4. De-carbonise transport fleets, e.g. through electric vehicles;
5. Offset emissions from corporate travel, e.g. through afforestation;
6. De-carbonise supply chains and helping customers lower their carbon intensity;
7. Advocate for regulations which drive the de-carbonisation of their industry to ensure its sustainability.

Voting

1. **We will typically vote against all directors of companies which do not publicly disclose their emissions and do not have a credible plan for their reduction.**
2. **We will also vote against auditors where the Annual Report and Accounts fail to report material climate risks.**

Divestment

We will also evaluate divestment where a portfolio company refuses to disclose its emissions and does not have a credible plan for their reduction.

Moody's disclosure to CDP

We are pleased to see that Moody's has provided disclosure to CDP for 2018 and 2019 (and since 2010) and we have carefully analysed these submissions.

However, for 2018, CDP awarded Moody's only an overall D grade. In our view, this is a highly unsatisfactory score. Moody's is a world class company and should be achieving an A grade rating, which represents best practice environmental stewardship and disclosure. (Please see the Appendix for CDP's guidance on how to achieve an A grade). Peer company S&P Global was rated A- in 2018. Please see the Appendix for guidance on how to become A grade.

In our view, it is untenable for Moody's to achieve such a low score when seeking to demonstrate environmental leadership through Moody's Investors Service and Moody's Analytics. It may also leave Moody's at a competitive disadvantage relative to peers.

In our recent calls and meetings, you have been confident that the CDP score of Moody's 2019 submission will show some improvement on the 2018 score, although it is very unlikely you will achieve the required A grade rating. We will actively monitor your progress and hope you can achieve a material improvement in 2020.

Moody's shortcomings and TCI requirements

While we are encouraged to see the creation of a CSR Council for Moody's which should help to coordinate environmental performance and disclosure across the company, based on our analysis of the CDP 2019 submission, there remain several significant shortcomings in Moody's climate-related disclosure and initiatives:

1. You should use climate-related scenario analysis to inform your business strategy, although we note that you anticipate doing so in the next two years;

2. No emissions targets are set for the business, although again, you anticipate doing so in the next two years. Moody's must set ambitious, science-based targets in emissions reductions;

3. Moody's should implement best practices for the sourcing and management of energy across all buildings, processes and transportation. For example, Moody's should join the RE100 initiative which commits participating companies to procure 100% of their electricity consumption from renewable sources;

4. Senior management and staff should be incentivised to deliver emissions reduction targets on a timely basis with a meaningful percentage of incentive compensation tied to these targets;

5. The submission suggests there is no engagement in activities that could influence public policy on climate-related issues given the need to be "sensitive to potential conflicts of interest" with the work of Moody's Investors Service. However, Moody's is in a very strong position to change corporate behaviour towards the management of climate-change related risks and improved disclosure, and should be doing so.

ESG leadership is a business imperative and commercial opportunity

We recently attended your ESG conference in London, and we were impressed by the event. It is clear you have increased your expertise in this area over the past few years through business acquisition and internal investment:

- Moody's Investor Services ESG research and credit ratings;
- Moody's Analytics, for example, via the Global Heat Map initiative;
- Acquisition of Vigeo Eiris the ESG research, data and assessment business;
- Green Bond Assessments.

We believe the deep integration of ESG analysis is a commercial imperative for Moody's as:

1. It will become increasingly important to the credit rating process as climate risks accelerate and governments respond to those risks through regulation and taxation;

2. ESG standard setting and research leadership is emerging as a highly valuable commercial opportunity as it integrates into the decisioning process of asset managers.

Rating agencies have a key role to play in ESG analysis for investors. Therefore, Moody's must continue to invest in making its ESG offering best in class. Failure to lead in ESG will compromise ratings performance and forgo business opportunities.

Moody's must strongly advocate for mandatory public disclosure of GHG emissions

Transparency is the bedrock of good investment decisions, and Moody's is a powerful stakeholder in the ecosystem. While we accept that in the ratings process, Moody's Investor Services (MIS) is often in possession of material non-public information (MNPI), which it cannot publicly disclose without the agreement of the issuer, this should not preclude advocacy for greater disclosure.

However, Moody's must be a robust private and public advocate for comprehensive GHG emissions disclosure from all companies that it rates, so that all investors across the capital structure can make informed decisions about the climate risks involved in investing in businesses.

MIS should recommend that all companies submit emissions data to CDP, so there is a common framework for comparison

CDP recently analysed submissions from 215 of the world's 500 largest corporations and found that these companies face $1tn in costs related to climate change in the decades ahead, unless they take proactive steps to prepare. By the companies' own estimates, a majority of those financial risks could start to materialize in the next five years.

The importance of incorporating emissions analysis into credit ratings is illustrated by the following examples:

1. The bankruptcy of Pacific Gas and Electric (PG&E), an investment grade rated company, whose exposure to the increasing frequency of California wildfires ultimately overwhelmed the business;
2. The Volkswagen Emissions scandal. VW illegally concealed true emissions performance of the automotive fleet which resulted in $30bn of fines and penalties;
3. Transactions like Fiat Chrysler and Peugeot are strongly motivated by the inability of some automobile companies to meet emissions standards standalone;
4. Alphabet has commented that rising temperatures may increase the cost of cooling its data centres;
5. Airlines such as IAG and Lufthansa will face significant investment demands to meet net zero carbon emission targets;
6. Fossil fuel-based energy companies in the coal, oil and gas, steel and cement industries are facing accelerating emission-based taxation and technology disruption from renewable energy sources.

A core business imperative of MIS is ratings accuracy. We have met with heads of a number of the rating divisions and it was evident to us that incorporating emissions data is seen as important to the accuracy of corporate credit ratings. While this is positive, the process needs to accelerate. A key message from your ESG conference is that investors are now demanding the disclosure of accurate and standardised environmental data.

<u>Moody's must advocate for banks to disclose climate change risks associated with their loan books</u>
We would like to make a specific comment on banks because they are a material part of the debt universe but offer extremely poor disclosure of their climate change risks. Investor exposures to climate change risks are leveraged in the banking sector.

Currently, nearly all banks refuse detailed public disclosure of their loan books and the associated climate change risks. While rating agencies (including Moody's) are typically provided with some of this information, clients of Moody's have limited ability to understand the underlying data behind the credit rating of the bank. In order to provide their clients with the highest quality credit analysis, Moody's should be advocating for banks to disclose climate change risks associated with their loan books.

We appreciate the time and effort Moody's has made incorporating ESG into its business. We look forward to continuing our dialogue.

Yours sincerely,

C. Hohn

Chris Hohn | Philip Green | Alex Baring

Appendix - How to become an A grade company in the CDP Climate Change Program

An "A grade" is the highest overall CDP score achievable and demonstrates a company's:

- Strong industry leadership on environmental actions and stewardship;
- Thorough understanding of the risks and opportunities related to climate change;
- Alignment with TCFD disclosure recommendations.

CDP uses its scoring methodologies to incentivise companies to measure and manage environmental impacts through participation in CDP's climate change, water, forests and supply chain programs. Scoring provides a roadmap for companies to achieve best practice.

Companies are assessed and scored across four consecutive levels, as the company moves towards strong environmental stewardship. Minimum scores must be achieved in order to move to the next level. Inclusion on CDP's A grade list requires a high leadership score.

The levels are:

1. Disclosure – every question is scored for quality and depth of disclosure, e.g. emissions, targets, environmental impact, strategy, governance, engagement;
2. Awareness – depth of analysis and understanding on how environmental issues affect the business;
3. Management – Evidence of actions taken to address environmental issues;
4. Leadership – Actions represent best practice as formulated by organizations working with CDP to advance environmental stewardship (e.g. Science Based Target initiative, CEO water mandate, CERES, WWF).

Help and guidance

CDP documents available to companies on the CDP website:

1. Scoring Introduction 2019
2. Climate Change 2019: General Scoring methodology Category Weightings

Specific guidance can be obtained from the **CDP Reporter Services Group**, for example, on how to improve the quality of disclosure and the actions required to demonstrate improvement.