18th July 2021

RE: Transition Pathway Initiative Response to the TCFD Forward-Looking Financial Sector Metrics Consultation

Dear Sir/Madam,

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Chair:
Professor Lord Stern
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We are responding to your consultation on two documents: *Proposed Guidance on Climate-related Metrics, Targets, and Transition Plans* and the associated *Measuring Portfolio Alignment: Technical Supplement*. We are members of the research team for the Transition Pathway Initiative (TPI) at the Grantham Research Institute on Climate Change and the Environment, London School of Economics. Backed by asset owners and supported by asset managers representing $30 trillion of combined Assets Under Management and Advice, TPI assesses the progress that companies are making on the transition to a low-carbon economy, supporting efforts to mitigate climate change. Our research also underpins the Climate Action 100+ Net Zero Company Benchmark. The TPI framework is designed to be aligned with the recommendations of TCFD. The TPI company assessments are based on companies' public disclosure and are published via an open-access online tool: www.transitionpathwayinitiative.org

Please note that this is a technical submission focused specifically on metrics and targets, section C and D of the *Proposed Guidance on Climate-related Metrics, Targets, and Transition Plans*. Please note that this submission is complementary to the one submitted by Asset Owner members of TPI on the 15th of July[1].

TPI has now developed sector benchmarks and frameworks for 10 major sectors (diversified mining; energy: oil and gas, electric utilities; transport: airplanes, automobiles, shipping; industrials and materials: aluminium, cement, paper, steel) and has conducted detailed Carbon Performance assessments of nearly 300 companies across these sectors. Within this Carbon Performance framework, we translate emissions targets made at the international level under the 2015 UN Paris Agreement on climate change into benchmarks, against which we compare the performance of individual companies. For each company, we create an emissions pathway spanning the last c. five years and going out to as late as 2050, based on its historical emissions and activity data, and on its announced targets. This experience has given us unique insights into the practical challenges of analysing corporate data, both for direct benchmarking/comparison and for the development of more complex metrics of corporate and portfolio performance.

[1] See further https://www.transitionpathwayinitiative.org/publications/86.pdf?type=Publication

Our experience has demonstrated that we urgently need a standardised framework defining how companies present their carbon data, and the supplementary information that needs to accompany these disclosures. Without this foundational framework in place, it is extremely difficult to robustly assess and compare company practice and performance. It also means that more sophisticated indicators and metrics simply add confusion and not clarity. The consequence is that, in the absence of such a framework, the core goal of TCFD, namely to produce climate-related financial data that can be used by market participants, simply will not be delivered. We present a mock-up of this template applicable to all sectors in Appendix 1.

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1. **Overall remarks:**

- We share the view of the TCFD that climate-related disclosure practices have evolved and the use of disclosure by financial and non-financial organisations has increased in recent years. In this regard, we welcome the TCFD efforts to: (i.) provide general guidance for organizations seeking to establish relevant metrics, targets, and transition plans around their climate-related risks and opportunities, and (ii.) propose specific changes to the Guidance for All Sectors and Supplemental Guidance in the 2017 TCFD *Final Report* and *Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures*.
- In this context, we recommend that the TCFD explicitly supports those forward-looking metrics that are already being widely used in the investment community for engagement and for investment analysis. In particular, we point to the TPI methodology assessing companies' governance and management of climate change issues under our Management Quality framework, and, as already mentioned, our Carbon Performance framework for quantitative benchmarking of companies' emissions and emissions targets (see: https://transitionpathwayinitiative.org/publications/65.pdf?type=Publication), as well as the Climate Action 100+ Net Zero Benchmark indicators that TPI provides (see https://www.climateaction100.org/wpcontent/uploads/2020/12/Net-Zero-Benchmark-Indicators-12.15.20.pdf).
- In this submission, we want to draw your attention to the need to take a comprehensive approach to corporate emissions target disclosure. **Based on our experience in analysing company disclosure across 10 high emitting sectors, and from our ongoing efforts to develop Carbon Performance methodology for new sectors, we have observed that companies take advantage of loopholes that exist because of the freedom they have to choose boundaries for emissions reporting whilst rarely disclosing information on which boundaries were chosen. ESG investing is hindered by the unclarity on target boundaries not allowing investors to assess a) the true magnitude of the companies low carbon transition ambitions b) dependence of these plans on the company's external**

actors through the use of offsets. Unclarity of target boundaries also means that it is often difficult, if not impossible, to compare targets on a like for like basis.

- **To address these loopholes, we propose that in revision of its guidance on targets, the TCFD focuses on four dimensions: GHG boundary, activity boundary, organisational boundary and use of offsets.** The emissions targets should be disclosed in a manner in which all four target dimensions are disclosed unambiguously. From our experience, a failure to disclose properly even one of the target dimensions can seriously undermine an assessors' ability to determine the company's intended low carbon efforts and by extension the company's transition risk. Ambiguity in any of the dimensions can also undermine an investor's ability to compare targets on a like for like basis.
- Specifically, we propose the revised TCFD guidance recommending companies disclose:
  A. **[GHG boundary] information on the types of GHGs covered by their emissions reduction targets/ambitions**;
  B. **[activity boundary] the business activities covered by emissions reduction targets/ambitions, including with respect to type (production/sales) and geographical range (worldwide/regional)**;
  C. **[organisational boundary] the organisational boundary that applies to their GHG emissions reduction targets/ambitions;**
  D. **[expected use of offsets] the amount of offsets expected to be used between the base year and the target year as well as in the final year in their GHG emissions reduction targets/ambitions.**

A rationale for the proposed recommendations is presented in the following section.

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2. Specific remarks on the GHG Target Disclosure template proposed by TPI

A. GHG boundary – which types of greenhouse gases are covered by the target?

Rationale: Many companies do not explicitly state whether their emissions reduction targets include certain types of emissions. For example, in the oil and gas sector, we – TPI – have assessed one company, which up until earlier this year limited its emissions reduction target to CO2, thus excluding non-CO2 GHGs such as methane, despite methane emissions being material in the sector in which it operates. Likewise, many companies in the food processing sector report emissions from purchased goods and services (i.e. agricultural products), without being explicit on whether these figures include emissions from land use, land-use change and forestry (LULUCF), which again are highly material. We also find that "carbon neutrality" targets often fail to account for non-CO2 GHG emissions. Therefore, **our first proposal is to include under the TCFD framework a**

recommendation for companies to disclose the types of GHGs covered by their emissions reduction targets.

B. **Activity boundary** – If the target does not cover the company entity as a whole, which of the company's activities are covered? Is the target limited to activities in a particular region? If the target covers some form of scope 3 emissions, how do the company's activities relate to its scope 3 target?

Rationale:

In practice, we find that some companies include only a limited number of activities related to their products in their target, e.g., only upstream activities in the oil and gas sector. The activity boundary can be further constrained when targets of a company operating worldwide are only regionally defined. Another layer of complexity is added by some targets being restricted to the company's own production activities, whereas other targets apply to company sales. For example, in the US power market it is common for electricity utilities to both generate and re-sell purchased electricity to consumers. The emissions intensity targets on a production basis, as opposed to sold electricity basis, may imply different transition strategies and transition risk. This example also highlights the fact that a lack of proper disclosure of a company's activities becomes especially challenging in the case of emissions intensity targets, which are based on a company's activity. Emissions intensity targets are very common. **Our second proposal is to include under the TCFD framework a recommendation for companies to disclose the business activities covered by emissions reduction targets/ambitions, including with respect to type (production/sales) and geographical range (worldwide/regional.**

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C. **Organisational boundary** – On which accounting boundary is the target set: the equity share, financial control or operational control approach?

Rationale: Companies can report information about their business using various different organisational boundaries. In the GHG reporting space, the two most common methods are the "financial or operational control boundary" (accounts for 100% of the emissions of assets controlled by the company and 0% of emissions of non-controlled assets) and "equity boundary" (accounts for emissions from all assets in proportion to the company's ownership share regardless of operational control). In practice, we find that companies often fail to disclose the organisational boundary of historical emissions data or their targets, especially regarding scope 3 emissions. This information is critical and the lack of it can misinform investors. To highlight the scale of this issue, we have encountered companies whose scope 1 emissions on an equity basis are just half of their operational emissions. **Our third proposal is to include under the TCFD framework a recommendation for companies to disclose the organisational boundary that applies to their GHG emissions reduction targets/ambitions.** A complementary recommendation could set an expectation on companies to disclose targets in a consistent manner by using the same organisational boundary in historical data and forward-looking targets.

D. **Use of offsets** – To what extent is the target set to be met through the use of offsets? What types of offsets does the company plan to use?

Rationale: In the context of the recent increase of corporate net-zero targets, the focus on companies' use of offsets has increased. Whilst in principle the use of offsets can be a cost saving mechanism enabling a cost-efficient transition on a whole-economy level, many important challenges remain in the implementation of offset markets. Therefore, transition plans heavily relying on offsets rather than on a company's own emissions present a different transition risk profile compared to those focused on own emissions. Hence, it is critical for investors to understand how extensively a company relies on offsets to achieve its targets. There are two key components to understanding the use of offsets in emissions targets. One is the overall use of offsets between the base year and the target year, while the second is the amount of offsets used in the final year. The former should be regarded as a minimum requirement and where possible companies should disclose expected use of offsets on an annual basis for all years between the base and target year. The latter metric, i.e., the use of offsets in the target year is important to understand the extent to which a company will transform its business by the target year and as a corollary by how much emissions could increase in the year following the target year. **Our fourth and final proposal is to include under the TCFD framework a recommendation for companies to disclose the amount of offsets expected to be used between the base year and the target yar as well as in the final year in their GHG emissions reduction targets/ambitions.**

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We hope that our recommendations on the corporate target disclosure together with the annexed GHG target disclosure template will be useful. We remain at your disposal should any clarification be needed to inform further your consultation process.

Yours faithfully,

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Appendix 1

GHG target disclosure template				
Target ID				Comments
Overall number of **active** GHG emissions targets	**4**			Include interim targets in the count
Target number:	**1 (of 4)**			
Target type:	**Absolute**			
Date the target was set:	**19/20/2020**	Date that the target was last revised:	**14.01.2021**	Indicate whether this is an interim target (e.g., a short-term milestone between the organization's mid- or long-term target and current period)
Organisational (accounting) boundary on which target is set	**Operational accounting boundary**			Please note any additional exclusions if any
Target GHG Information				
Scope(s) covered	**Scope 1 & 2 (market-based) + 3 (cat 11: use of sold product)**			For scope 2 emissions, indicate if calculations are location- or market-based. For scope 3 emissions, indicate the GHG protocol categories that are covered.
Greenhouse gases covered	**CO2, CH4**			
Base year:	**2015**	Base year emissions:	**75 000 tCO2e**	
If intensity target: provide activity measure	**2015**	Base year activity:	**250 000 mboe**	For intensity targets, provide activity measure (e.g., tCO2e/MWh or tCO2e/tonne of cementitious product)
Target year:	**2030**	Target year projected emissions:	**30 000 tCO2e**	
Targeted reduction from base year (%)	**60%**			
Targeted reduction from current year (%)	**50%**	Current emissions:	**60 000 tCO2e (2020)**	Please indicate the most current year for which emissions data is available.

Target Activity Information		
Activities covered	Barrel oil equivalent of crude oil and natural gas produced by the upstream business in Europe	Please note regional applicability of the target if not global
Target Activity Information (If intensity target)		
Activity metric	gCO2e/mboe	
Base year activity	250 000 mboe	
Offsets		
Specify whether the use of offsets is included in the target	Yes/No	
Amount of [proportion if intensity target] targeted emissions reductions the company expects to be met by using offsets covering the entire time frame between the base and target year	10%	For intensity targets please provide the percentage as the difference between the average intensity over the target period with the use of offsets and without. (ie. the difference between the average gross and average net target as percent of the average gross target)
Amount of [proportion if intensity target] targeted emissions reductions the company expects to be met by using offsets in the final year of its targets/ambitions	4%	For intensity targets please provide the percentage as the difference between the intensity in the final year with and without the use of offsets (ie. the difference between the gross and net target as percent of the gross target)
Types of offsets used	Nature based solutions, emissions reductions	
List of offset suppliers allowed under the target	Gold Standard, Verra	
Target Methodology		
Source describing decarbonisation strategy outlining how this target will be met.	**Roadmap to Net-zero 2050 (p.1 -10)**	

For Scope 3 targets, a source describing the methodology used to calculate the Scope 3 emissions covered by the target.	**GHG Emissions Methodology (p.15-16)**
For net emissions (eg. net-zero) targets, indicate the share of emissions reductions through offsets and provide a source describing their type.	**20% will be achieved through CCS. Roadmap to Net-zero 2050 (p. 8)**
For intensity targets, a source describing the methodology used to calculate the carbon intensity.	**Sustainability Report 2020 (p.89)**