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Transition Plan Taskforce: a sector-neutral framework for private sector transition plans

ClientEarth response to May 2022 Call for Evidence

Classification: Internal

ClientEarth

About ClientEarth

ClientEarth is an international non-profit environmental law organisation headquartered in London. Our team of Climate Finance lawyers are global experts in the field, focusing on the legal implications of climate change-related risks and impacts for a wide spectrum of market participants, including banks, companies, investors, directors, professional advisers and regulators.

This document responds to the Transition Plan Taskforce's call for evidence (the **TPT**, and the **TPT CfE**) regarding the development of a sector-neutral framework for private sector transition plans.

We would welcome further discussion with the TPT on any of the topics below.

Executive summary

The purpose of the TPT sector-neutral framework must be to establish a rigorous best-practice baseline for transition plans which are aligned with climate science and the climate goals enshrined in the Paris Agreement not only on paper but in practice. A sufficiently robust framework should help stimulate genuine transition, stamp out 'greenwashing' and transition 'in name only', and ensure that promised actions are actually taken, not just disclosed. The opposite is true of a framework which is compromised from the outset.

We consider the following elements to be absolutely critical to the design of a framework which supports corporate and financial institution ambition and action on climate change:

- **Science-based, Paris-aligned ambition**. Company climate targets, emissions trajectories and plans must be compatible with a 1.5 °C low or no-overshoot scenario by 2050, consistent with the Paris Agreement. On a cross-sector global basis, this implies absolute emissions reductions of 45% by 2030 (which corresponds to a linear annual reduction of 4.2%). The minimum expectations for ambition should evolve with the latest climate science. **See our responses to questions 16 and 19.**
- **Comprehensive emissions inventories and targets**. Companies should include all of the emissions associated with their operations and value chains (including Scopes 1-3) in their transition plans. Data gaps are not an excuse for material gaps in the plan, and best estimates should be used where necessary. **See our responses to questions 15 and 19.**
- **Prioritise absolute emissions reductions**. Companies must prioritise absolute emissions reductions. Emissions intensity targets can only be an optional additional metric and cannot replace absolute emissions reduction targets. **See our response to question 16.**
- **Short- and medium- term action is essential.** Rapid and deep emissions reductions are necessary before 2030. Company plans must include concrete short- and medium- term action to cut their absolute emissions, recognising that in some cases this will involve trade-offs for the business. Companies must set emissions reduction targets for 2025 and 2030 at the latest, to be reviewed every five years. **See our responses to question 15 and 19.**
- **'Offsets' cannot be relied upon**. If companies use 'offsets' to achieve their emissions reduction targets, transition will be undermined. GHG removals, carbon credits and avoided emissions may only be disclosed separately as other 'contributions' and must not obscure the company's absolute emissions reductions. **See our responses to questions 16, 19 and 20.**
- **Paris-aligned lobbying**. Companies' direct and indirect lobbying must be aligned to the goal of halving emissions by 2030 and reaching global (net) zero by 2050. **See our response to question 19.**
- **Consistent accounting.** Companies must take account of climate related risks and any commitments made in their transition plans in their accounts. The impact on the accounts, and any estimates, assumptions and judgements made in them must be transparently disclosed (including any capital expenditure necessary to deliver the plan) so that investors and other stakeholders can make informed financial decisions. Misaligned accounts may indicate greenwashing, and obscure financial risk. **See our response to question 9.**

- **Accountability.** Merely having a transition plan is not enough. It is crucial that companies and financial institutions deliver against their plans and are held to account for the quality and implementation of their transition plans by regulators, investors, NGOs and other stakeholders. Regulators are currently failing to hold companies to account for the sustainability and climate-related disclosures they are already required to make[1] and must step up their enforcement to support effective transition. Although enforcement mechanisms in the relevant regulations will be essential, the TPT framework itself must be designed from the outset to support the necessary accountability. Anchoring transition plans in the latest climate science, and the most credible available emissions reduction pathways is essential as it will enable users to assess whether companies' plans are aligned with the goals of the Paris Agreement. We also support the inclusion and strengthening of any elements of the framework which will enable companies to be effectively held to account, including: short- term target setting, regular monitoring and reporting (including on the fulfilment of promised actions *and* granular KPIs), aligned remuneration and incentives, and named-director accountability for the delivery of the transition plan. **See our response to questions 16 and 19.**

Finally, we would support changes to the framework to better integrate Just Transition principles, and to acknowledge the interdependencies between climate and other sustainability factors such as nature and biodiversity, including the need for transition to be achieved in a way that does not significantly harm such other factors.

ClientEarth's response to the TPT CfE questions

Questions on Section 1: Introduction to the TPT

(1) Do you agree with the proposed definition of a transition plan? If not, why, and what alternative definition would you suggest?

We do not agree with the proposed definition of a transition plan in its current form. In our view changes are required to ensure the framework is sufficiently robust and to align the definition with the principles set out on page 12 of the TPT CfE.

By permitting companies to set their own level of climate ambition, the definition is fundamentally unfit for the purpose of driving change to the status quo where high-emitting company emissions targets and capital expenditures are not aligned with the 1.5C pathways which match the UK's own legal obligations.[2] This approach is more likely to hinder than to drive net zero transition, and risks perpetuating existing greenwashing behaviour and effects. It will also feed the perception of the UK as a 'light green' or even 'grey' financial centre, in contrast to the emerging standards focussed on 1.5C pathways at the EU level.[3]

[1] See ClientEarth, Accountability Emergency: A review of UK-listed companies' climate change-related reporting (2019-20) (2021).
[2] See CA100+, '*Climate Action 100+ Net Zero Company Benchmark Shows An Increase In Company Net Zero Commitments, But Much More Urgent Action Is Needed To Align With A 1.5°C Future*' (March 2022).
[3] See EFRAG's draft climate change reporting standard ESRS E1 (published in April 2022), available here.

In our view, science-based emissions reduction pathways with a reasonable likelihood of achieving the 1.5°C temperature goal of the Paris Agreement with little or no overshoot should be baked into the heart of the transition plan framework, including the definition. This will support the development of transition plans which are sufficiently robust and aid regulators and stakeholders to hold to account those who present insufficient plans.

It should also be made clearer that businesses may be required to fundamentally change the way they operate in order to achieve global climate goals (e.g. in some cases the absolute emissions required by the applicable pathway will only be possible by reducing output in a particular business line) – they are not merely required to adapt as necessary to survive economically in a world that is transitioning around them, without addressing their own contribution to the climate crisis. Including references to climate *impacts* (as well as risks) and the capital expenditure necessary to achieve transition in the definition will help clarify the scope of the necessary change.

We have suggested several changes to strengthen the proposed definition, as follows:

> "*A transition plan sets out how an organisation will adapt its business model and strategy and reduce its emissions consistently with the global transition pathways necessary to limit global warming to 1.5°C in line with the Paris Agreement, as the world transitions towards a low carbon economy. It should set out a) ~~high-level~~ short- and medium-term targets the organisation is using to mitigate its climate risk and impact, including absolute greenhouse gas reduction targets ~~(e.g. a net zero commitment)~~, b) interim milestones, and progress made against those targets and milestones; c) how those targets and milestones are aligned with global transition pathways (and, if applicable, sectoral transition pathways) to achieve the Paris Agreement temperature goal, d) actionable steps the organisation plans to take to hit those targets; and e) how the transition plan will be funded, including through necessary capital expenditure.*"

We would also welcome further changes to the definition to recognise the need to consider Just Transition principles and the impact of the organisation on wider sustainability factors including nature and biodiversity.[4]

(2) From your perspective, who are the key users of transition plans?

The key users of transition plans include:

- **Corporate boards and financial institution executives** needing a reference point for the design and implementation of transition plans and strategies, and the necessary organisational change.
- **Shareholders and investors** wishing to allocate capital to finance transition and / or hold the company or financial institution to account in relation to its approach to climate change through informal and formal engagement, voting at AGMs and, in some cases, litigation to address legal non-compliance and / or recover losses, including:
  - **institutional investors** (including pension funds) discharging their own fiduciary and regulatory responsibilities through asset allocation, stewardship and engagement;
  - **retail investors, consumers and other beneficiaries** choosing which company or institution to invest or save with based on its approach to climate change;
  - **debt finance providers** including banks and alternative credit providers;
- **Regulators** policing compliance with transition plan disclosure requirements and the quality of plans, and seeking to counter 'greenwashing';

[4] See our response to question 5 for more detail.

- **Employees** and prospective employees;
- **Non-governmental organisations** (**NGOs**) seeking to assess and support or challenge (as needed) companies' approach to climate change;
- **Other financial sector actors** who assess financial and other types of risk, including: insurers, credit and ESG ratings agencies, traders and proxy advisors.

(3) From your perspective, what are the key use cases for transition plans?

Our response to question 2 mentions some of the key use cases for transition plans.

Crucially, transition plans must: (a) drive organisational change within companies and financial institutions necessary to address accruing systemic transition-related financial risks; (b) provide settled clarity to consumers and investors so that they can make informed purchasing and investment decisions rather than reacting to events on the basis of unclear and shifting disclosures on transition issues; and (c) create an environment in which companies and institutions are held accountable for both their approach to climate change, and the public claims they make about it.

There are also likely to be benefits to providing companies with a clear articulation of best-practice standards for transition plans and a degree of legal certainty (through the corresponding regulatory framework) regarding the standard to which they will be held. However, this will only be achieved if the best-practice framework itself is sufficient to drive companies to achieve the Paris Agreement temperature goals on the basis established by the best climate science currently available.

Finally, the TPT transition plan framework must embed appropriate standards and requirements into the UK regulatory regime for corporates and financial institutions in order for the UK to deliver on its commitment to be the first net-zero financial centre, and set an appropriately high benchmark for other regulators and standard setters to follow globally.

(4) How should the TPT select which sectors to develop tailored transition plan templates for? Following that logic, what financial sub-sectors and real economy sectors should the TPT prioritise? In what order should these be addressed?

In the real economy, we would suggest that the TPT should prioritise those sectors which produce the most greenhouse gas (**GHG**) emissions, and which face particular challenges to effective transition. Globally, this would mean the following sectors: energy supply, industry, agriculture, forestry and land use (**AFOLU**), transport and buildings.[5] In the UK this would mean: transport, energy supply, business / industrial, residential and agriculture.[6] However we would suggest that the TPT should be guided by sources of global emissions given that the UK financial sector's global financed emission are likely far greater than UK domestic emissions. International aviation and shipping must also be prioritised to the extent they do not otherwise fall within the "transport" sector.[7]

It may also be appropriate to prioritise industrial sub-sectors such as steelmaking, cement and chemicals, which have particularly high emissions and are required to urgently decarbonise, play a key

[5] As of 2019. See paragraph B.2.1 of the IPCC's AR6 WGIII Summary for Policy Makers (February 2022), available here.
[6] As of 2020. See Figure 5 on page 14 of the UK Department for Business, Energy & Industrial Strategy's (**BEIS**). '*2020 UK Greenhouse Gas Emissions, Final Figure*s' (February 2022), here.
[7] Emissions from aviation and shipping are the fastest growing source of EU GHG emissions. See EU Parliament, '*Emissions from planes and ships: facts and figures (infographic)*' (December 2019), here.

'up-stream' role in the value-chain in relation to other sectors and / or face particular challenges to effective transition.[8]

Given the magnitude of the global "financed emissions" of the financial sector[9], and the critical leverage held by financial institutions over financed companies, it is also essential that robust transition plan templates and methodologies are established for financial institutions as soon as practicable, including:

- Bank lending and investment banking;
- Insurance;
- Regulated / retail investment funds;
- Private / alternative investment funds, including private credit funds, infrastructure and property funds and private equity; and
- Pension providers.

Although financial sector transition is largely dependent on the implementation of real-economy transition plans, we do not consider that financial sector transition frameworks should be delayed until all key real-economy sectors have been addressed, as this delays essential action by financial sector actors to use their influence to accelerate real-world transition, though allocation decisions and forceful engagement and stewardship.

The financial sector frameworks must comprehensively cover global financed emissions to capture the most material climate impacts (and risks) associated with the relevant institutions. Given the direct link between loan financing and access to liquidity and cost of capital (including for project-specific financing) there may be an argument for prioritising banks and other providers of debt finance on the primary markets (including loans and bonds) over other types of institutions in the short-term.[10]

It is important that financial sector transition plans indicate what institutions should do to accelerate transition in the real economy including, for example: robust stewardship and voting based on investee company transition commitments; allocation decisions including financing for activities that support transition; and the imposition of transition-related conditions on loan and bond financing and refinancing. They must also implement transition strategies for financing carbon-intensive sectors, including using their own demanding sectoral transition pathways so that transition planning at financial institution level supports the transition required at real economy sectoral level. Related to this, financial institutions must rule out the financing of activities known to be fundamentally incompatible with the Paris Agreement goals.

Given that detailed templates for some sectors and sub-sectors will not be developed until later in the 'critical decade for accelerated action'[11], it is essential that the sector-neutral framework is ambitious and robust enough to support necessary transition across all sectors in the meantime, by reference to the cross-sectoral pathways established by the Intergovernmental Panel on Climate Change (**IPCC**) and other organisations such as the Science Based Targets Initiative (**SBTi**).[12]

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[8] For example, the decarbonisation pathways modelled by BEIS require the UK iron and steel sector to be "largely decarbonised by 2035". See the BEIS '*Industrial Decarbonisation Strategy*' (March 2021), here at page 53.

[9] The UK finance sector's financed emissions were over 700x greater than its direct emissions in 2020: see CDP, '*The Time to Green Finance*' (April 2021), here. It has been estimated that financing by UK banks and investors is responsible for 1.8 times the UK's annual domestic carbon emissions (which would make the City of London the ninth largest emitter of carbon dioxide in the world, if it were a country): See WWF and Greenpeace, 'The Big Smoke: the global emissions of the UK financial sector' (May 2021), here.

[10] See, for example, the Oxford Sustainable Finance Group's paper on '*Sustainable Finance and Transmission Mechanisms to the Real Economy*' (Caldecott et al, April 2022), which concludes that loans are the most 'high-impact' asset class.

[11] See paragraph 18 of the Glasgow Climate Pact.

[12] See footnote 39.

(5) Given the mandate set out in the TPT's Terms of Reference, to what extent, and how, should the TPT consider issues beyond a firm's contribution to an economy-wide decarbonisation? Why?

The IPCC is clear that an effective transition is a just and equitable transition.[13] The TPT should consider how Just Transition principles are reflected in the sector-neutral framework, alongside the firm's contribution to economy-wide decarbonisation, to ensure that progress on climate targets does not come at the expense of a fair transition for workers. We welcome the inclusion of "alignment with Just Transition" principles as an element of the framework, but this could be supported by more granular disclosure requirements and / or more integration with other elements in the framework.

It is also essential that the framework take due account of sustainability factors beyond climate change, including nature and biodiversity. We support calls for transition plans to include targets and safeguards to ensure that corporate transition strategies do not significantly harm nature in other respects. This is also essential given the interconnections between nature and climate change, including (a) the contribution to greenhouse gas emissions from the destruction of natural ecosystems; and (b) the role of nature in climate change mitigation, adaptation and resilience.[14]

(6) Which of these issues are 'must-haves' that need to be addressed in all transition plans, and which are 'desirable', which add depth or breadth but are not central to a transition plan?

We consider an appropriate approach to the above issues to be essential to all transition plans.

(7) Do you envisage any tensions between entity-level decarbonisation and economy-wide decarbonisation goals? If so, can you provide examples and any suggestions as to how the UK TPT may address these in its guidance.

There are several potential tensions between entity-level and economy-wide decarbonisation goals:

- **Interpretations of 'net zero' and use of offsets**. Companies are currently using the broad concept of reaching 'net zero' emissions to obscure their lack of commitment to the rapid and deep absolute emissions reductions that are necessary to meet the Paris Agreement climate goals. By focusing on their emissions intensity (rather than absolute emissions reductions) and in appropriately 'balancing' GHG removals, avoided emissions or carbon credits against the emissions they produce (rather than making absolute emissions reductions), companies are able to give the appearance of 'carbon neutrality' or having mitigated their climate impact. However, given the need for absolute emissions reduction globally across the economy, this is deeply misleading and harmful. As the IPCC has stated, "*modelled pathways that limit warming to 2°C (>67%) or lower share common characteristics, including rapid and deep GHG emission reductions. Doing less in one sector needs to be compensated by further reductions in other*

[13] See paragraph TS-5 of the IPCC's AR6 WGIII Technical Summary (February 2022), available here.
[14] See, for example, the recognition of these interactions in the Glasgow Leaders' Declaration on Forests and Land Use (COP 26, 2021), here.

sectors if warming is to be limited. (high confidence)"[15] The TPT framework can address this confusion and reduce the space for greenwashing by demanding rigour and holding companies to transition plans that prioritise absolute emissions reductions which align to credible emissions reduction pathways consistent with the Paris Agreement.

- **Fundamentally incompatible activities**. There are some activities that are known to be fundamentally inconsistent with achieving the Paris Agreement goals. This includes any investment in new oil and gas development and investments in thermal coal.[16] However, companies and institutions involved in conducting or financing these activities currently get away with publicly committing to support transition, without committing to wind-down such activities or financing in the manner required by to meet the Paris Agreement. The TPT must require companies and financial institutions to disclose their involvement in such activities, the locked-in carbon associated with them, and the company's strategies to wind them down or otherwise deal with them. Otherwise, a focus on numerical emissions reductions will continue to distract from the fundamental trade-offs necessary to achieve transition.

- **Financed emissions and financial sector decarbonisation**. Although it is essential that financial institutions measure and address their 'financed' or 'insured' emissions, it is important that the transition plan framework does not create perverse incentives for institutions to decarbonise their portfolios by simply 'tilting' their portfolios towards lower carbon investments through allocation and divestment decisions at the expense of real-world decarbonisation. Instead, institutions should be incentivised to use their leverage to accelerate transition in the real economy through engagement, stewardship, voting, and ultimately financing and divestment decisions (including the financing of activities which actively support transition).[17]

(8) What other financial or non-financial, mandatory or voluntary frameworks and processes are you aware of that the TPT should consider as it proceeds?

In addition to the sources already reviewed, we suggest that the TPT also have regard to:

- The draft climate change reporting standard ESRS E1 published by the European Financial Reporting Advisory Group (**EFRAG**), which includes disclosure requirements for transition plans, climate targets, energy consumption and GHG emissions and other information points.[18]
- The guidance on climate action plans provided by the Say on Climate initiative[19], including the Children's Investment Fund Foundation's (**CIFF**) presentation on the essential components of a corporate climate action plan.[20]
- The efforts of the Our2050world initiative, led by BSI, ISO and the Race to Zero Campaign, to develop a set of Net Zero Guiding Principles.[21]

[15] See C.3.1 of the IPCC AR6 Summary for Policy Makers.
[16] Under the IEA's net zero by 2050 scenario, no new oil and gas development is required beyond 2021. See footnote 33.
[17] See ClientEarth's 'Principles for Paris-alignment' (October 2020). For an example of the nuanced debate about the value of a financed emissions-based approach see, for example, the Climate Risk Review's recent article 'Has the backlash against financed emissions begun?' (July 2022).
[18] EFRAG's draft climate change reporting standard ESRS E1 (published in April 2022) is available here.
[19] The Say on Climate guidance on climate action plans is available here (accessed 6 July 2022).
[20] CIFF's July 2021 presentation on the essential components of a corporate climate action plan is available here.
[21] Details of the Our2050world initiative are available here (accessed 6 July 2022).

- ClientEarth's October 2020 position paper on Principles for Paris-alignment, which may be a useful source of additional guidance.[22]
- The UN Secretary-General's High-Level Expert Group on the Net-Zero Emissions Commitments of Non-State Entities.[23]
- The IIGCC's net-zero investment framework and implementation guide.[24]

Questions on Section 2: The Sector-Neutral Framework

(9) Where would you prefer for companies to disclose information on their transition plans? Please explain your reasoning, including on how the suggested location relates to the intended audience.

Transition plan disclosures should be made in such a way and in such location as to provide as much transparency as possible to all of the stakeholders identified in our response to question 2.

Primarily, companies should include their transition plan disclosures in the 'front end' of their annual report, rather than in a separate document. Where applicable, the disclosures should be included alongside the other non-financial and sustainability information (including climate information) disclosed in the company's strategic report. It is also essential that the transition plan disclosures are integrated with both: (a) any other narrative reporting on climate risk provided by the company in the 'front end' of its annual report; and (b) the company's financial statements.

In order for investors and other stakeholders to make fully informed assessments of a company's approach to climate change, they must be able to access in one place disclosures covering the company's business strategy and transition plans, climate-related risks and impacts, and financial position.

Moreover, it is vital that the financial information included in company financial statements incorporates proper consideration of climate-related risks and any climate or transition related plans and commitments made by the company, and their impact on the company's financial position, in a manner which is clear and transparent, and that this information is subjected to adequate audit scrutiny. Without this information, climate change will not be effectively incorporated into financial decision-making because the financial impact on the company of transition will be obscured.

This information is material to investors who have repeatedly called for climate considerations to be integrated into company financials.[25] Accounting and audit standard setters have also clarified that, where climate risks are material, they should be taken into account in preparing company financial statements and audits.[26] However, these standards are not being met in practice.[27] Unless the transition plan framework ensures that a company's commitments to transition, along with any identified climate-

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[22] ClientEarth's 'Principles of Paris-alignment' are available here.
23 The High-Level Expert Group's website is available here.
[24] IIGCC's implementation guide is available here.
[25] See, for example: IIGCC, Investor Expectations for Paris-aligned Accounts (2020); Sarasin & Partners, Investor Expectations: Net-Zero Audits (2021); and IIGCC, Investors put Audit Committee Chairs on notice over continued omission of climate risks in financial reporting ahead of 2022 AGM season (2022).
[26] A full discussion of accounting and audit standards, investor requests to companies and auditors as regards financial reporting, and the apparent failure to meet such standards can be found on the website of the UN Principles for Responsible Investment, here (accessed 6 July 2022).
[27] See the findings of Carbon Tracker and the Climate Accounting Project, Flying Blind – the glaring absence of climate risks in financial reporting (2021) and ClientEarth, Accountability Emergency: A review of UK-listed companies' climate change-related reporting (2019-20) (2021).

related risks, are reflected in its financial statements, investors and other stakeholders will be left in the dark about the financial implications of company transition plans. It will also help to weed out greenwash, as it should be impossible for companies to make commitments in their transition plans whilst accounting on an inconsistent basis that assumes that the Paris Agreement temperature goals (or their own corporate commitments) will not be achieved. The current practice of aspirational 'net zero' ambitions which are not integrated across financial information is a clear driver of accruing financial, regulatory, litigation and systemic risks.

The TPT's sector neutral framework should include an explicit requirement for the impact of the transition plan on the company's financial position (including specific estimates, assumptions and line items) to be transparently disclosed in the notes to the company's accounts. Users of accounts must be able to see what the company's ambitions and strategy mean for its balance sheet.

However, recognising the density and complexity of the narrative reporting already provided by companies under existing requirements, key information about the company's transition plan should be clearly disclosed on the company's website and periodically shared with investors, in addition to its inclusion in the annual report.

(10) How prescriptive should the Sector-Neutral Framework be, recognising the need to balance flexibility in how firms disclose transition plans with more prescriptive templates that seek to facilitate comparability of firms' transition plans?

A degree of prescription is necessary to ensure that transition plans are: (a) as consistent and comparable as possible; and (b) rigorous enough to support companies in a transition that is consistent with the Paris Agreement temperature goals.

Allowing too much flexibility for companies to set their own targets and pathways, without due regard for climate science, would make the TPT sector-neutral framework unfit for the purpose of decarbonising corporate emissions and would be disastrous for the climate and the economy.

Key points where prescription is required (each of which is discussed in more detail in our responses to questions 15 to 20, below) include:

- the need for companies to align their targets, emissions trajectories and plans with a 1.5 °C low or no-overshoot scenario by 2050, consistently with the Paris Agreement goals, rather than allowing them to define their own aspirations freely;
- the requirement for companies to include in their plans all of their emissions from their entire business and value chain, including Scope 3 (save for immaterial exclusions - meaning <1% of the company's total emissions inventory);
- preventing inappropriate reliance on 'offsets' to achieve emissions reduction targets, which would fundamentally undermine the rigour of the framework; and
- explicit requirements for the commitments made in the transition plan to be 'carried over' into the company's financial statements, and for the impact on the financial statements to be clearly disclosed.

(11) Should the TPT seek to standardise the data and metrics used to communicate ambition and measure progress in transition plans? If so, what are the standards for data and metrics that you would recommend including in the Sector-Neutral Framework and in supplementary sectoral guidance?

We have no substantive comments in response to this section, save that it is essential that robust standards and metrics are formulated independently of any undue influence from the corporations and entities which will be subject to transition plan requirements and might seek to limit the rigour of the regime overall.

(12) Question for small and medium-sized enterprises: what specific challenges do you foresee for SMEs seeking to prepare or use transition plans? How can the guidance and framework prepared by the TPT address these concerns?

We have no comments in relation to this question.

(13) Question for preparers only: if your firm does not already disclose information of the type outlined in this Call for Evidence, what are the reasons for that? For example, are there concerns about legal or possible market risks arising from disclosure? How could the work planned by the TPT address these concerns?

We have no comments in relation to this question.

(14) Transition plans provide an opportunity to ensure the benefits of the climate transition are widely felt by UK households and consumers. How can the guidance developed by the TPT balance the need to minimise costs whilst encouraging companies to develop strategies to maximise benefits for all?

The primary benefits of limiting global heating to 1.5°C for the planet and all its people are clear.[28] There is also potential for transition to have significant economic benefits for individual companies and also for sectors, regions and communities, for example through scaling up cheap green energy sources or creating new green jobs locally. In addition, it is increasingly clear that consumers and retail investors wish to spend and invest in a more sustainable way. There are inherent benefits to providing reliable and

[28] The IPCC's October 2018 '*Special Report on Global Warming of 1.5°C*' set out the deep and widespread impacts which an increase in the global average temperature of 1.5°C would be likely to cause, and highlighted the significant differential in impacts between 1.5°C and 2°C of global average warming – see the Summary for Policy Makers.

comparable information that enables them to do so, which in turn will shift spending patterns and financial flows to support transition.[29]

Nevertheless, we are in a corporate transition crisis, in that the status quo allows for companies to transition 'in name only'. Information asymmetries and a lack of consensus on what a credible transition plan involves allows 'greenwashing' by companies which are not Paris-aligned, which contributes to the accrual of significant financial and systemic risks.

Climate science is clear that "*all global modelled pathways that limit warming to 1.5°C (>50%) with no or limited overshoot, and those that limit warming to 2°C (>67%) involve rapid and deep and in most cases immediate GHG emission reductions in all sectors*".[30] However, while many companies have some kind of net zero goal, very few have short-term emissions reduction targets and even fewer plan capital expenditure or draw up financial statements consistently with net zero.[31] The Bank of England has noted that only a limited share of UK firms "*publish comprehensive, consistent and comparable reports on their targets, actions and investment plans*" and commented on the negative impact this has on reliable market pricing of risk.[32]

Alongside the introduction of mandatory transition planning requirements through regulation, the TPT framework needs to solve this problem by requiring companies to disclose comprehensively and clearly against a rigorous framework aligned with a 1.5°C temperature rise. By stimulating genuine transition, the framework will contribute to benefits for all. Continuing to support weak and misleading transition plan disclosures will have the opposite effect, slowing progress, building stranded asset risk, and preventing consumers and retail investors from making more sustainable purchasing and investment decisions in line with their preferences.

(15) Do you agree with the proposed principles? Why or why not?

Broadly, we welcome the three principles set out in the Call for Evidence. However, we believe that these need to be strengthened in key respects:

- **Principle 1. *Align with an economy-wide net zero transition*** should be strengthened to state that targets, emissions trajectories and plans must be compatible with a 1.5 °C low or no-overshoot scenario by 2050, rather than making this merely an "ideal" option. The second sentence should require that the company's targets, emissions trajectories and plans should cover all of its emissions, in particular Scope 3. It is important that this Principle also recognises that, separately to acceptable emissions reduction trajectories, there are some activities which companies simply must not engage in or fund if they are to align their plans with economy-wide net zero transition, including those identified in the International Energy Agency (**IEA**) net zero by 2050 scenario for the energy sector.[33] Bluntly, an investor who is told that a company involved in any way in coal, oil or gas expansion has a 'net zero transition plan' is likely being misled.

[29] See, for example, Deloitte, '[How consumers are embracing sustainability]' (2022) (accessed 13 July 2022): "*Our research shows that consumers are increasingly making conscious decisions with sustainability and the environment in mind. However more needs to be done to give consumers greater access to information and offer better affordability and availability of sustainable options*."
[30] See paragraph C.3 of the IPCC AR6 Summary for Policy Makers.
[31] See footnote 2.
[32] See pages 11 and 16 of Bank of England, '*Options for greening the Bank of England's Corporate Bond Purchase Scheme*' (May 2021).
[33] The IEA's 'Net Zero by 2050 Roadmap', published in May 2021, stated that there must be no new oil and gas fields, new coal mines, coal mine extensions, or new unabated coal plants approved for development after the time of publication if net-zero is to be reached by 2050.

  - For financial institution transition plans, Principle 1 should include an additional "sub-principle" that targets, emissions trajectories and plans should cover the entirety of the institution's "financed" or "insured" emissions (as applicable).[34] Although we acknowledge that TPT plans to develop sector specific guidance for the financial sector in a subsequent phase of work, we suggest this sub-principle is included in the sector-neutral framework from the outset given the damaging consequences of delay in the publication of sector-specific proposals.

- **Principle 2. *Focus on concrete actions which emphasise the near-term and are backed up by clear governance mechanisms*** should be strengthened by requiring interim targets to be set for 2025, 2030 and reviewed at a maximum of five-yearly intervals after that to set clearer expectations on the requirement for action in the near- and medium-term. The requirement for companies to explain how their actions are "in line with the transition to a net zero economy" should be amended to refer back to a 1.5 °C low or no-overshoot by 2050 scenario, consistently with Principle 1. The second sentence of Principle 2 should be amended to require integration into, and coherence with the accounting estimates, assumptions and judgements used in preparing the companies accounts. It should also be amended to refer to plans being backed up by clear governance, *incentives and accountability* processes.

(16) Are there any principles that you would add to the list above? Why?

The following principles should be added to the call for evidence:

- **'Offsetting' may not be relied upon.** GHG removals, carbon credits and avoided emissions should not be relied upon to meet the targets, emissions trajectories or plans set by the company. If used, these should be disclosed separately to the company's Scope 1-3 emissions and reduction targets as other 'contributions'. If GHG removals, carbon credits or avoided emissions are relevant to the company, it should provide sufficient disclosure for an informed assessment of their credibility to be made.[35]

  It is essential that GHG removals, carbon credits and avoided emissions are not used inappropriately as 'offsets' in a way that undermines the absolute emissions reductions necessary to achieve global climate goals, or presented misleadingly to investors or consumers as reducing a company's emissions or neutralising its climate impact.[36] This principle must be

[34] For further commentary, see ClientEarth's 'Principles for Paris-alignment' (October 2020) which require that "*financial institutions must disclose a policy which explains how they will influence reductions in their Scope 3 GHG emissions through investment, stewardship, financing and underwriting decisions, in order to achieve their targets*".

[35] See the position taken by EFRAG on GHG removals, carbon credits and avoided emissions in its draft climate change reporting standard ESRS E1. See Disclosure Requirements E1-3 and E1-12 to 14. The commonly used corporate net zero standard designed by the SBTi also restricts the use of carbon credits in achieving emissions reduction targets. See SBTi, Science-Based Net-Zero Targets: 'Less Net, more Zero' (2021).

[36] Achieving climate goals requires the significant reduction of emissions year on year, and we have no 'room' in the global carbon budget for incurring avoidable emissions on the basis that they are balanced by offsets. As put by Carbon Watch in its Carbon markets 101, *"in order to be able to offset one's emissions, someone else needs to have "extra" emission reductions available to sell. Yet, the Paris Agreement requires all countries to reduce emissions as much as they can. This means that there is no room to offset, because there are no "extra emission reductions" available when countries are already doing their maximum"*. The Voluntary Carbon Markets Integrity Initiative concludes in its 2021 consultation report that *"The imperative for overall and absolute emissions reductions globally, to keep 1.5˚C within reach, necessarily means the end to 'traditional' offsetting"* at page 31.

baked into the sector-neutral transition plan framework from the outset so that GHG removals, carbon credits and avoided emissions are not used to meet emissions reduction targets.

- **Prioritise absolute emissions reductions.** Company targets, emissions trajectories and plans should prioritise absolute emissions reductions by 2030 wherever possible and disclose corresponding absolute emissions reduction targets. If used by the company as an additional metric and target, emissions intensity must be reported separately from the firm's primary absolute emissions metrics.

  It has been established beyond doubt that achieving the 1.5 °C temperature goal of the Paris Agreement with low or no-overshoot requires deep and widespread absolute emissions reductions to begin immediately, without which, the global carbon budget will be depleted before 2030.[37] It is essential, therefore, that companies align their transition plans with the global effort to reduce emissions by 45% by 2030.[38] The SBTi has determined that on a cross-sectoral basis, this requires emissions reductions at a linear annual rate of at least 4.2%.[39] While some credible sector-specific pathways will vary from this (and may in certain circumstances permit a focus on emissions intensity reductions), the assumption for the sector neutral framework should be that companies will align their targets and plans with these trajectories unless there is an extremely good reason to take a different approach.

- **Consistency.** The targets, commitments and plans made in a company's transition plan should integrated and consistent with the company's business and investment strategies, governance and accountability processes, remuneration structures and the estimates, assumptions and judgements used in preparing its accounts.

  As noted above in our response to question 9, this is essential to prevent companies using published transition plans as an opportunity to greenwash, and to enable investors and other users of corporate reporting to make fully informed financial decisions on the basis of accounts which reflect the impact of the company's commitments on climate change. Given the importance of this requirement, TPT should consider creating a separate consistency principle. However, we have also suggested similar changes to the existing Principle 2 in our response to question 15.

- **Accountability**. Transition plans must ensure that there is meaningful accountability for the company's transition. At a minimum, companies should name a director who will be responsible and accountable for the design and implementation of the transition plan, and explain how incentives are aligned with the successful delivery of the plan.

- **Take account of nature.** We support calls for the inclusion of an additional principle requiring the transition plan to do no significant harm to nature, for the reasons set out in our response to question 5.

[37] The Glasgow Climate Pact recognises that "*limiting global warming to 1.5 °C requires rapid, deep and sustained reductions in global greenhouse gas emissions, including reducing global carbon dioxide emissions by 45 per cent by 2030 relative to the 2010 level and to net zero around mid-century, as well as deep reductions in other greenhouse gases*" (paragraph 22).
[38] The IPCC has shown that pathways with a reasonable chance of limiting warming to 1.5 °C require global net CO2 emissions to be reduced compared to a 2019 baseline by 48% in 2030 - see paragraph C.1.2 of the IPCC's AR6 WGIII Summary for Policy Makers (February 2022), available here. Net global greenhouse gas emissions must fall by 43% by 2030 – see paragraph C.1.1.
[39] See pages 15 and 25 of SBTi's 'Corporate Net Zero Standard' (October 2021).

(17) Which of these principles would you regard as 'must-haves' or as 'desirable'?

We regard all of the principles set out in the Call for Evidence, and our additional principles as essential. This is because the additional principles are directly informed by our experience of existing problems in current corporate practice. Leaving transition plan 'loopholes' (offsetting, intensity targets, incomplete emissions inventories, exclusions etc.) will simply encourage further greenwash.

(18) Principle 1 notes that a transition plan should cover the whole organisation. There may be challenges for internationally active firms in meeting Principle 1, given that different jurisdictions will have different economy-wide transition pathways.

How can the TPT design its standard and guidance in a way that accommodates credible transition plans consistent with the broader strategy of a firm, but reflects differences between approaches taken in different jurisdictions?

In our view, the primary objective of the TPT should be to set a world-leading best-practice standard for the design and assessment of transition plans, to drive equivalent ambition globally. Concerns about convergence should not detract from the level of ambition at this stage.

As explained elsewhere in our response to question 10, a certain degree of prescription on key elements (Paris-alignment, full emissions inventory including Scope 3, no reliance on 'offsets', consistency with financial statements etc.) is essential to uphold the rigour of the framework.

This level of prescription will also help guide the approach to jurisdictional differences. The starting assumption should be that companies should align their plans with sector-wide pathways to achieving the 1.5 °C low or no-overshoot scenario by 2050.[40] Any deviations from this trajectory which reduce the level of ambition required from the company must be: (a) strictly necessary under applicable sectoral or national scenarios; (b) minimised to the extent possible; and (c) rigorously justified and disclosed.

There may be cases where the applicable sectoral or jurisdictional framework requires an accelerated transition, in which case companies should align their plans to the higher standard and explain the basis for doing so.

Finally, linkages between transition planning, other sustainability factors including nature and biodiversity and Just Transition principles, may require or help explain modifications to the cross-sectoral pathway in certain circumstances. Acknowledging this in the framework should help ensure that such factors are meaningfully considered by companies, and this should be transparently explained in the plan where relevant.

[40] See also our proposed additional principle *Prioritise absolute emissions reductions* in our response to question 16.

(19) Do you agree with the proposed elements? Why or why not?

Overall, we welcome the attempt by TPT to synthesise the elements set out in existing transition plan guidance and current FTSE company practice and, taken together, we find the proposed elements encouraging. However, in order to ensure that the sector-neutral framework is fit for purpose and does not facilitate greenwashing, we have the following comments on the elements currently proposed:

- **Interim targets and dates / Target year and GHG emissions.** Should specify that the company must set absolute[41] emissions targets for 2025 and 2030, to be reviewed every five years.

- **Baseline year and GHG emissions.** Should specify that:

  (a) companies should use a 2019 baseline year and emissions to set their targets to enable users of transition plan disclosures to compare the company commitments with the emissions reduction pathways set out in the IPCC's Sixth Assessment Report[42]; and

  (b) companies should include in their GHG emissions all sources of emissions which fall into GHG Protocol Scopes 1, 2 and 3[43] unless they are non-material (meaning <1% of the company's total emissions inventory). If the precise number for a particular source of emissions is unknown, companies should use best estimates and clarify any data gaps (including their size relative to known emissions).

- **Scope of business activities covered.** Should specify that companies must set (territorial, entity- and activity-based etc.) boundaries that cover their whole business and value chain, unless any exclusions are immaterial. Best estimates should be used if needed.

- **Alignment with temperature trajectory / transition pathways**. Companies should explicitly disclose whether their emission reductions are aligned with the trajectories established by the IPCC for a reasonable likelihood of achieving 1.5°C consistently with the goals of the Paris Agreement.[44] If not, companies should clearly warn users of this fact, disclose the reasons, and explain how their plans would need to change to be so aligned.

- **Reliance on offsets**. Reliance on 'offsets', and the three other elements relating to offsets should not be included in the *Target Setting* section of transition plans. Taking this approach in the TPT's best-practice framework risks encouraging companies to rely on offsets to formulate and achieve their emissions reduction targets. As noted in our response to Question 16, use of offsets to 'address' emissions alongside or in replacement of reductions is one of the key barriers to decision-useful information on transition plans, and would undermine achieving the 1.5 °C

[41] Intensity targets are an optional additional metric. In some sectors and circumstances, intensity targets may provide additional relevant information, in which case they may also be disclosed *if deemed meaningful*, Currently, intensity targets are too often used to obscure failures to reduce – and even growth in – absolute emissions. Intensity targets must not replace absolute emissions reduction targets. See para. 24 of Disclosure Requirement E1-3 in EFRAG's draft climate change reporting standard for a comparable approach.
[42] See footnote 38. If 2019 is not a genuinely representative baseline year, then a company may use an alternative recent baseline year or average baseline year range which is genuinely representative of its typical emissions profile. For example, COVID-19 may mean that 2020 and 2021 are not representative. For a comparable approach, see the SBTi Corporate Net Zero Standard, at page 20.
[43] See the GHG Protocol Corporate Standard, here.
[44] See footnote 38 and the text to footnote 39 for the precise implications of this on a cross-sectoral basis.

temperature goal globally. This would also diverge from the approach taken in EFRAG's climate disclosure standard, creating confusion for users and contributing to the perception and reality of the UK as a 'light green' financial centre in contrast to the EU as a net zero financial centre.

Instead, GHG removals, carbon credits and avoided emissions should be dealt with as separate '*contributions*' to climate change mitigation that do not 'offset' the gross emissions of the company.[45] Following the approach currently proposed by EFRAG, GHG removals, carbon credits and avoided emissions should be disclosed and reported upon separately (including from each other) in a discrete section of the transition plan and a separate line of the *Metrics and monitoring progress* section, and not conflated with emissions reduction KPIs which show how the company is progressing against its targets.

Within this structure, we agree that companies should demonstrate the credibility of the '*contributions*' chosen, including the type of contribution and the rationale for its selection over other options, third party verification and assurance that carbon credit projects avoid local social and environmental harms.

- **Engagement: public sector & industry peers**. Companies must ensure that direct and indirect lobbying is aligned to the goal of halving emissions by 2030 and reaching global (net) zero by 2050.[46] Even if the company's own targets are less ambitious, the company's lobbying should still support the more ambitious global pathway.

(20) Are there any elements that you would add to the list below? Why?

We suggest adding the following elements to the proposed list:

- **Contributions**. As noted in our response to question 19, we consider the inclusion of 'Offsets' in the *Target Setting* section to be deeply problematic. A separate element on 'Contributions' should be included instead, ensuring that GHG removals, carbon credits and avoided emissions are disclosed and considered separately to the company's primary emissions reduction targets and pathways.
- **Plans to address incompatible activity and investment.** We suggest an additional element is included in the *Ambition* section requiring companies to disclose their involvement in any assets or activities known to be fundamentally inconsistent with credible pathways to achieving the 1.5 °C temperature goal (or investment therein), the proportion of the company's activities or revenues attributable to such activity (or investment), the locked-in emissions associated with such assets or activities, and how the company plans to phase out its exposure to such activities as required by the relevant pathway. This would include, for example, any investment in new oil and gas development and investments in thermal coal.[47] There is a risk that companies pursuing business models fundamentally incompatible with the Paris Agreement are able to obscure that fact by focusing on more abstract emissions reduction targets in their disclosures, and this element seeks to address that risk.
- **Financial plan.** We agree with the existing components of the proposed financial plan disclosures. However, companies should also be required to:

[45] For this reason, we consider use of 'offsets' as an umbrella term to be misleading.
[46] See the 'Persuade' section of the updated 2022 updated Race to Zero criteria, here (accessed 7 July 2022).
[47] Under the IEA's net zero by 2050 scenario, no new oil and gas development is required beyond 2021. See footnote 33.

(a) explicitly confirm in their transition plans that their financial accounts incorporate the impact of the climate commitments made by the company in its transition plan;

(b) provide cross references to the notes in the accounts which explain how climate related factors have been incorporated into estimates, assumptions and judgements, and any line items which have been specifically affected[48]; and

(c) explain how their CAPEX and OPEX plans are consistent with a 1.5 °C aligned strategy, identifying any inconsistencies.[49]

- **Risk factors**. It should be clarified in the *Management activities and plans* section that companies should identify and assess the principal risk factors to achievement of the plan in a manner consistent with the disclosure of principal risks and uncertainties in the strategic report, and how they will be addressed. Similarly, the impact of implementation of the transition plan on the company's principal risk and uncertainty position should be transparently disclosed. Risk factors should include the locked-in GHG emissions from key assets and products, including an explanation if and how these can jeopardise the achievement of GHG emission reduction targets and drive transition risk.[50]
- **Board accountability**. In addition to the existing board oversight and board approval elements, it should be clarified that overall responsibility for climate change and the transition plan should be assigned to a named board director or directors. This would help investors use the director re-appointment votes as an accountability mechanism through voting at company AGMs.[51]
- **Financed emissions**. Within the *Target setting* section it should be clarified that financed emissions should be disclosed and included in emissions inventories and targets where relevant. This requirement would mainly be relevant to financial institutions but should be included in the sector-neutral framework in case of delay in the publication of finance-sector specific guidance by TPT. This element may also be relevant to corporate investment groups or sub-groups.[52]
- **Approach to nature and biodiversity.** Consistent with our comments in response to question 16, companies should be required to disclose how they have avoided any potential harm to nature from their transition plan and otherwise taken account of the opportunities and risks associated with nature (and biodiversity loss), including the linkages with climate mitigation and emissions reduction, and the company's impacts on nature and biodiversity.
- **Annual report on fulfilment of actions.** We would support an additional element in the *Metrics and monitoring progress* section requiring companies to produce an annual report on the fulfilment (or not) of the actions they commit to in their plan. Separately to any granular KPIs and

[48] The US Securities and Exchange Commission (**SEC**) has proposed a similar approach in its March 2022 Proposed Rules to Enhance and Standardize Climate-Related Disclosures for Investors, which include a series of specific requirements as to how the impact of climate change has affected a company's financial statements (including in some cases the effect of climate change on specific accounting line items). See the SEC Fact Sheet which accompanies the new rules for details.
[49] Including the funding of any activities incompatible with net zero by 2050 according to the IEA and any other authoritative sources.
[50] See para. 15(b) of Disclosure Requirement E1-1 in EFRAG's draft climate standard.
[51] See also Disclosure Indicator 8 of the CA100+ Net Zero Company Benchmark, and Principle 3 of ClientEarth's 'Principles of Paris-alignment'.
[52] As noted in footnote 34, we acknowledge the nuances to designing an appropriate approach to financed emissions that supports, and does not distract from, real-economy emissions reductions.

metrics that the company reports, this would help investors, regulators and other stakeholders understand simply whether to company has done what it said it would.[53]

(21) Which of these elements would you regard as 'must-haves' or as 'desirable' for credible transition plans? In which instances should an entity assess materiality to determine whether an element is considered must-have and/or what level of disclosure detail is required?

Subject to our comments in response to questions 19 and 20, we see all of the suggested elements of the sector-neutral framework as important.

(22) Are there elements where you see substantial barriers to implementation? If so, which ones and why? Are you able to suggest alternatives which are both credible and practical?

We anticipate that corporates will raise objections to a more prescriptive approach. The oft-cited reasoning is, however, flawed:

- **Data availability**. Current data gaps, for example regarding Scope 3 emissions, are not a valid basis for permitting the exclusion of material categories of emissions. Meaningful disclosure and proper management of financial risk requires that material sources of emissions are factored in, and this can always be done on an indicative, qualitative and/or estimated basis. As one example, oil and gas companies routinely exclude Scope 3 emissions from 'non-energy products', which omits the material Scope 3 emissions of large petrochemical production operations. Such emissions from the variety of uses of petrochemicals are difficult to measure precisely but can be estimated. As another example, airlines do not report the non-CO2 warming effects of aviation. The non-CO2 effects are challenging to measure precisely, but have been estimated at around 3x the CO2 warming effect of aviation since 2007.[54] The omission of the (larger) non-CO2 effects has led to an absence of corporate planning to mitigate these effects, increasing transition financial risks and causing shareholders to operate on materially incorrect information. Aviation non-CO2 effects should be clearly reported on an estimated basis and included in transition plans.[55]
- **Flexibility**. Whilst the framework must be flexible in application, it must not be flexible in ambition. The scientific imperative applies economy-wide and is very clear - the IPCC has highlighted that "*all global modelled pathways that limit warming to 1.5°C (>50%) with no or limited overshoot, and those that limit warming to 2°C (>67%) involve rapid and deep and in most cases immediate GHG emission reductions in all sectors*".[56] In our experience, operators in 'hard to abate' sectors can seek to make use of 'flexibility' which results in a transition plan which falls far short of net zero transition and so instead contributes to breaching agreed climate limits. Aviation, for example, argues that emissions reductions must be delayed in an attempt to block

[53] Note the similar suggestion on page 483 of the Climate Change Committee's recent report to Parliament (June 2022), here.
[54] See Atmosfair, 'The impact of air travel on our climate', here (accessed 13 July 2022).
[55] See CA100+'s March 2022 global sector strategy for the aviation section, here.
[56] See footnote 30.

demand-side mitigation to reduce air traffic.[57] This simply means that correspondingly greater emissions reductions will be needed elsewhere, but such 'adjustments' are not envisaged.[58]

(23) Please share any other feedback or comments you may have on the work of the TPT and the Sector-Neutral framework.

Please see the covering comments made in the *Executive Summary*.

For further information regarding anything covered in this response, please contact:

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[57] See Transport & Environment, '*Why "flying less" offers the best path to sustainable aviation*' (March 2022).
[58] See C.3.1 of the IPCC AR6 Summary for Policy Makers.

Classification: Internal