

Q1: Are there any specific data sources that might be useful for a historical analysis of transition risk for private and public equity and debt? How can EIOPA access them? Why are they relevant?

1. EIOPA's discussion paper ("DP") proposes to assess the impact of climate change transition risks on asset prices by conducting both a backward-looking analysis based on historic data and a forward-looking model assessment. We consider that there are significant issues with relying on historic data to assess the impact of transition risk exposures on asset prices, and that relying on such data may significantly underrepresent the impact of transition risks on companies and asset prices.
2. This is because the nature and scale of the future climate transition, and its impact on the economy and companies, will be significantly different to the impact that the transition has had historically. Rapid decarbonisation is needed in future to meet global climate goals, which means that the impact of transition risks on companies will not be linear. This is because: (1) in future there will need to be more rapid decarbonisation and more transformative policy change than in the past, in order to meet global climate targets; (2) certain sectors will need to decarbonise particularly rapidly in future in an unprecedented manner; and (3) the climate transition could lead to shocks to the global economy in future. We address each of these three points in turn below.

RAPID DECARBONISATION

3. In order to limit warming to 1.5°C or even to the "well below 2°C" goal of the Paris Agreement, far more severe and rapid global emissions reductions will be required in future than have occurred to date. In addition, there will need to be significant and rapid changes in policy in order to achieve this. The current policy response of global governments is consistent with 2.7°C warming.¹ In addition, the IPCC found that policies implemented up to the end of 2020 were on track to lead to 3.2°C warming.²
4. Accordingly, there will need to be a significant acceleration in emissions reductions by companies in future, and there will need to be much deeper and more transformative policy change in order to achieve this. The transition risks faced by companies will therefore be much greater than those they have faced in the past.
5. We note that the DP recognises that the future climate transition may differ to the transition to date, and that there may be more significant and rapid policy action by governments in future. The DP states that a limitation of using historic data on transition risk is that there has been "*Absent or subdued policy action to foster the economy's decarbonisation until recent years*". In addition, the DP proposes that EIOPA's forward-looking analysis will assess various transition scenarios, including a disorderly transition scenario which assumes a delayed and then rapid policy response (although the DP states that this scenario is considered to be low probability). As the current policy response is already delayed and inconsistent with global climate goals, unprecedented rapid and transformative policy change is a significant risk in future, and this should be reflected in EIOPA's analysis.

¹ Climate Action Tracker, 'Temperatures'.

² AR6 WGIII SPM C.1 found: "*Without a strengthening of policies beyond those that are implemented by the end of 2020, GHG emissions are projected to rise beyond 2025, leading to a median global warming of 3.2 [2.2 to 3.5] °C by 2100 (medium confidence)*".

IMPACT OF TRANSITION ON PARTICULAR SECTORS

6. Net-zero emissions pathways for certain sectors will require particularly rapid decarbonisation in future, as well as the exclusion and phase out of certain activities in an unprecedented manner. Consequently, the impact of the climate transition in those sectors will be markedly different to the transition's impact to date.
7. The fossil fuel sector provides an example of a sector that must implement significant change, and unprecedented decarbonisation, in order to align with global climate goals. The UN Environment Programme has modelled that, in order to limit warming to 1.5°C, there must be significant annual reductions in thermal coal, oil and gas production (11%, 4% and 3% respectively) up to 2030.³ However, it also found that the sector is far off track to meet such goals, as governments are currently planning more than twice the amount of fossil fuel production in 2030 than is consistent with limiting warming to 1.5°C.
8. In addition, the International Energy Agency's ("IEA") net-zero pathway in its Net-Zero by 2050 report set out timelines for the phase-out of fossil fuel production and found that there must be no new coal mines and oil and gas fields developed (beyond those approved as of 2021) in a pathway consistent with limiting warming to 1.5°C.⁴ However, energy majors continue to expand fossil fuel production and develop new mines and fields.
9. Given the significant and rapid change to fossil fuel production that is required in future to align the sector with climate goals, future transition risks for the fossil fuel sector are far greater than historic transition risks. The impact of past transition risk exposures on historic past asset prices therefore may not be an accurate guide to the impact of future transition risk on future asset prices. In particular, companies engaging in new and expanded fossil fuel production will be subject to heightened transition risks, including the risk of stranded assets, in future (see our response to question 13 below for a summary of the risks of new fossil fuel activities).
10. We note that the DP recognises that the need for future change in the energy sector will impact the utility of historical data. It states that a limitation of using historical data on transition risk is that there has been a *"Historical paradigm of the world's energy needs being fulfilled using fossil fuels as primary energy source, despite corresponding environmental externalities, made the carbon footprint of firms a negligible aspect for investors over decades."*

ECONOMIC SHOCKS

11. The climate transition could lead to "green swan" events that cause unprecedented shocks to the global economy in future. For example, the Bank for International Settlements' report on green swan risks found that: *"Traditional backward-looking risk assessments and existing climate-economic models cannot anticipate accurately enough the form that climate-related risks will take. These include what we call "green swan" risks: potentially extremely financially disruptive events that could be behind the next systemic financial crisis"*.⁵

³ UN Environment Programme and others; 'The Production Gap 2021 Report' (October 2021).

⁴ International Energy Agency, 'Net Zero by 2050: A Roadmap for the Global Energy Sector' (2021) and 'World Outlook 2022' (November 2022).

⁵ Bank for International Settlements and Banque de France, 'The green swan: Central banking and financial stability in the age of climate change' (January 2020).

CONCLUSION

12. In view of the above, we consider that EIOPA should be cautious in relying too heavily on its backward-looking analysis based on historic data to assess the impact of transition risks on asset prices, and it should recognise that transition risks will be greater in future.
13. The DP notes that *“historical asset prices materialized under a different paradigm, as climate attributes were not nearly as relevant for asset prices as they will be according to the current trajectories of climate change”*. The DP therefore proposes to use forward-looking models to supplement the backward-looking analysis, but it intends to rely primarily on the backward-looking analysis. The DP states that the forward looking model will be *“used to cross-check and validate the findings from historical time series analysis, since assets with a material transition risk exposure in the past should also show a similar risk exposure at least in the short to mid-term perspective”*. For the reasons set out above, this approach may underrepresent the future impact of transition risk on asset prices.
14. Accordingly, we propose that EIOPA should take a precautionary approach to transition risk exposures when developing a dedicated treatment of assets associated with transition risk, which recognises that future transition risks may be different in nature and scale to past risks. In particular, we propose that investments in companies that are involved in the new exploration, expansion or development of fossil fuel projects and related infrastructure (**“New Fossil Fuel Activities”**) pose such heightened future transition risks that they should be given their own dedicated prudential treatment (see our response to question 13 below).

Q3: Do you have comments on the outlined criteria for the selection of market indices?

15. Sustainability market indices cannot be assumed to include only assets with low climate transition risk. The DP notes that each index has its own specific methodology on ESG issues, stating that *“market indices differ substantially regarding their methodologies, e.g. in terms of ESG-related criteria and their index weighting. Therefore, findings derived on market indices should be interpreted carefully for the purposes of a prudential risk assessment.”* We agree that it is important for EIOPA to be careful in using sustainability market indices as a proxy for low transition risk exposures, as there are limitations to the admissibility criteria and scoring methodologies used by such indices.
16. If EIOPA decides to use market indices to inform its transition risk exposure analysis, then it should, when selecting indices: (1) conduct its own assessment of whether indices’ admissibility criteria and scoring methodologies are effectively designed to accurately track companies that mitigate their climate transition risk; and (2) review the composition of indices to assess whether the application of indices’ criteria leads to them actually investing in companies with low climate transition risk (and excluding with companies with high transition risk) in practice.
17. In particular, when selecting market indices to use, EIOPA should assess whether the indices’ methodologies for tracking climate transition risk are consistent with climate science, including science-based cross-sector and sectoral decarbonisation pathways and timelines for phasing out particular carbon-intensive activities. Within the fossil fuel sector, the admissibility criteria and scoring methodologies should be consistent with the IEA’s net-zero pathway in its Net-Zero by 2050 report, including its timelines for the phase-out of fossil fuel production and its exclusion of the development of new coal mines and oil and gas fields.

18. Some sustainability indices have limited criteria in relation to fossil fuels that do not reflect sectoral decarbonisation pathways. For example, some indices have exclusions in relation to coal, but do not have any exclusions in relation to the expansion of oil and gas production (which is inconsistent with the IEA's pathway), which would allow investment in companies exposed to significant climate transition risk (see our response to question 13 below on the risks of new fossil fuel activities). In addition, 'multi-factor' indices may give too much weight to other factors (such as governance related matters) which allows for companies that should perform poorly on climate-related factors to be included.
19. The limitations in indices' admissibility criteria and scoring methodologies have to led real issues in practice. Indices labelled as 'ESG', 'sustainable', 'low carbon' or 'climate' which claim to include only companies that are aligned with global climate goals have nevertheless included companies whose activities are inconsistent with the climate transition, including companies that support the development of new coal mines and oil and gas fields. This may arise either as a result of the index methodology being inadequate, or due to inadequate application of the index's own rules. For example, four MSCI climate indices included the company Adani Ports and Special Economic Zone (APSEZ) (which was linked to the controversial Adani Carmichael coal mine in Australia), although after being prompted to perform a review, MSCI revised APSEZ's 'controversy score' and excluded the company from these indices.⁶ To take another (non-MSCI) example, the FTSE Developed ESG Low Carbon Select Index has included shares in Glencore, Rio Tinto and BP.⁷ Sustainability indices therefore cannot be assumed to accurately measure transition risk, and any information that EIOPA obtains from such indices must be rigorously assessed against EIOPA's own analysis of transition risk.

Q13: Would you have suggestions for sector definitions other than by NACE code? What are their advantages? How does one quantify their transition risk?

20. The NACE codes include classes for specific fossil fuel sectors, which would clearly be sectors with high transition risks.⁸ However, they do not distinguish between companies that are involved in the new exploration, expansion or development of fossil fuel projects and related infrastructure ("**New Fossil Fuel Activities**") and those fossil fuel companies that are not involved in such activities.
21. We consider that companies undertaking New Fossil Fuel Activities pose such heightened transition risks that they should be given their own dedicated prudential treatment. In particular, we support the "One-for-one" campaign which calls for investments in such companies to be subject to a 100% capital requirement, and we also propose that they should be excluded from the matching adjustment.⁹ We

⁶ Market Forces, '[Adani Ports kicked off MSCI indices due to Carmichael coal link](#)' (26 November 2021).

⁷ FTSE [Developed ESG Low Carbon Select Index website](#) lists its holdings (accessed 10 January 2023). Note that the index includes investments in Glencore and Rio Tinto, despite specifically claiming to exclude "*companies identified as involved with thermal coal extraction and electricity generation*".

⁸ In particular see: groups 06 - extraction of crude petroleum and natural gas; 09.10 - Support activities for petroleum and natural gas extraction; 05 - Mining of coal and lignite; 35.21 - Manufacture of gas; 19 - Manufacture of coke and refined petroleum products; 20.11 - Manufacture of industrial gases.

⁹ ClientEarth, [Letter to European Commission in support of enhanced capital requirements for fossil fuel-related assets and liabilities](#) (9 July 2021); ClientEarth, [Response to the UK government consultation on Solvency II](#) (July 2022); [letter from a coalition of NGOs \(including ClientEarth\) to the President of the European Commission and others on the "One-for-one" campaign on fossil fuel capital requirements](#) (27 October 2021); ClientEarth, [Feedback to European Commission Solvency II proposals](#) (January 2022).

note that the Basel Committee on Banking Supervision has set prudential standards for cryptoassets that imposes a one-for-one capital requirement for certain cryptoassets in recognition of the degree of risk in such exposures,¹⁰ which may be a useful reference for adopting a similar approach in relation to New Fossil Fuel Activities.

22. We therefore consider that EIOPA should assess the risk of investments in companies that undertake New Fossil Fuel Activities in its transition risk exposures analysis. If a sector specific approach is taken to quantifying transition risks for EIOPA's transition risk exposure analysis, then additional sector categories should be included for fossil fuel companies which undertake New Fossil Fuel Activities. We summarise the risks of New Fossil Fuel Activities below.

RISKS OF NEW FOSSIL FUEL ACTIVITIES

23. New Fossil Fuel Activities are fundamentally incompatible with the goals of the Paris Agreement including limiting warming to 1.5°C above pre-industrial levels (the “**Paris Goals**”),¹¹ as well as the EU Commission's 2030 Climate Target Plan and its aim for the EU economy to reach net-zero emissions by 2050.
24. Almost 40% of *existing* global ‘developed’ fossil fuel reserves (from existing and under construction oil and gas fields and coal mines) need to be left unextracted in a science-based pathway aligned with 1.5°C,¹² so the exploitation of *new* reserves cannot be permitted in any reasonable science-based pathway. For example, the IEA's landmark report on net-zero pathways indicates that, in order to limit warming to 1.5°C, there must be no new oil and gas fields approved for development and no new coal mines or mine extensions (beyond projects already committed as of 2021). This means that investment in oil and gas must be limited to existing production facilities or those already approved for development.¹³ Climate goals require an end to new development of oil and gas fields and coal mines.
25. As a result, investments in New Fossil Fuel Activities are exposed to significant climate-related transition risks that are not adequately reflected in current capital requirements. New Fossil Fuel Activities will lock in fossil fuel infrastructure for decades to come, and are based on the assumption that the assets will be economically viable throughout their projected lifetime. However, many of those assets will become stranded during their lifetime due the substantial transition risks they are exposed to:
- a. New Fossil Fuel Activities may become economically unviable due to the increasing impact of new laws and regulation, as national transition policies inevitably accelerate globally in order to meet the Paris Goals. For example, carbon prices are expected to rise significantly.¹⁴ These

¹⁰ Basel Committee on Banking Supervision, ‘Prudential treatment of cryptoasset exposures’ (December 2022).

¹¹ Articles 2(1)(a) and (c) of the Paris Agreement under the United Nations Framework Convention on Climate Change commit signatories (including the UK) to pursue efforts to limit warming to 1.5°C, as well as to aim to make finance flows consistent with a pathway towards low emissions.

¹² Kelly Trout et al, ‘Existing fossil fuel extraction would warm the world beyond 1.5 °C’, 2022 Environ. Res. Lett. 17 064010. See also Carbon Tracker, ‘Unburnable Carbon: Ten Years On’ (2022) which found that 90% of all known (or ‘proven’) fossil fuel reserves must remain unextracted in order to limit warming to 1.5°C.

¹³ University of Oxford, ‘Implications of the International Energy Agency Net Zero Emissions by 2050 Scenario for Net Zero Committed Financial Institutions’ (2022).

¹⁴ See the Principles for Responsible Investment, ‘The Inevitable Policy Response 2021: Policy Forecasts’.

risks are even greater if policy action is delayed, and is therefore introduced in a more sudden and disorderly manner, in order to make up for lost time.¹⁵

- b. New Fossil Fuel Activities are exposed to the risk of falling (and volatile) fossil fuel prices, in light of falling market demand as companies increasingly recognise the financial and reputational imperative to align their business models with Paris Goals, as well as competition from clean energy as technological developments reduce the cost of renewables and electricity storage.¹⁶

26. It is estimated that over \$1 trillion of oil and gas assets are at risk of becoming stranded,¹⁷ and energy majors have already had to write down significant amounts of assets due to these risks.¹⁸ The potential for such write downs not only poses risks for insurers investing in such assets, but also leads to the accumulation of systemic climate risk in the financial system. Such transition risks are by their nature complex and unpredictable, and yet can manifest in a short timeframe.

27. In addition, warming in excess of the Paris Goals gives rise to systemic risks for the insurance sector. Such systemic risk should be reflected in the capital regime, in order to ensure the long-term resilience of the insurance sector. Accordingly, the capital regime should support limiting warming to the Paris Goals. In particular:

- a. Climate change may lead to certain types of risk becoming uninsurable, as a result of either: (1) consumers being unwilling or unable to pay the increased level of premium that insurers require to accept the risk transfer (including as a result of increased reinsurance costs), such as homeowners who may be unable to afford the increased costs of cover in areas increasingly affected by extreme weather events;¹⁹ (2) insurers being unwilling or unable to accept the maximum possible losses arising from risks for solvency requirement reasons; or (3) insurers being unable to accurately estimate the frequency and severity of risks in order to price premiums, due to unpredictable and rapidly changing risks.²⁰ This poses a fundamental risk to the insurance industry, as it has been forecast that extreme warming would lead to a world that is largely uninsurable.²¹

¹⁵ See the Late Action scenario in the Bank of England, 'Results of the 2021 Climate Biennial Exploratory Scenario' (2022). See also Carbon tracker, 'Handbrake Turn' (2020).

¹⁶ See BloombergNEF, 'New Energy Outlook 2021'.

¹⁷ Carbon Tracker, 'Unburnable Carbon: Ten Years On' (2022).

¹⁸ Analysis by Carbon Tracker indicates that seven oil and gas firms wrote down assets totalling \$87 billion within a nine month period in 2019-2020, as reported in [the Guardian](#).

¹⁹ For example, the Australian Climate Council estimates that 1 in 25 homes in Australia will be uninsurable by 2030, due to the increased risks from extreme weather events (including flooding and wildfires) making cover unaffordable. See its media release, 'Climate Council Launches Cutting Edge Digital Climate-Risk Map' (2022).

²⁰ CRO Forum, 'The heat is on' (2019). These risks are recognised by regulators. See for example analysis in PRA, 'The impact of climate change on the UK insurance sector' (2015), EIOPA, 'Discussion paper on non-life underwriting and pricing in light of climate change' (2020), and IAIS and SIF, 'Issues Paper on Climate Change Risks to the Insurance Sector' (2018) which notes that insurers may face difficulty in accurately pricing climate-related physical risks, as the risks can change in non-linear ways. See Swiss Re, 'Socio-economic developments and climate-change effects to drive rising losses from severe weather events' (2020) which finds that unmitigated climate change could jeopardise the insurability of weather risks.

²¹ See CRO Forum, 'The heat is on' (2019) which finds "The 3°C scenario creates real insurability challenges and could therefore challenge the sector". See also statements by Henri de Castries (at the time, CEO and Chairman of AXA) that 4°C warming would lead to most assets being uninsurable (reported in [Environmental Finance](#) in 2015),

- b. Warming in excess of the Paris Goals poses significant macro-economic risks to insurers' asset portfolios that cannot be effectively managed through portfolio construction and asset allocation. Such macro-economic impacts will be irreversible and far-reaching in breadth and magnitude, causing a substantial reduction in global GDP compared to a Paris-aligned scenario.²²

Q15: Do you have any comments on the company-specific transition risk measures set out in this chapter? Are there other ones? If so, what are their advantages?

NEW FOSSIL FUEL ACTIVITIES

28. As set out in our response to question 13 above, New Fossil Fuel Activities pose heightened prudential risks. Accordingly, if an individual company approach is taken to EIOPA's assessment of transition risk, then the measures for assessing transition risk should take into account whether companies are involved in New Fossil Fuel Activities. As set out above, we consider that investments in such companies should be subject to a 100% capital requirement and should be excluded from the matching adjustment.

COMPANY EMISSIONS TARGETS

29. The DP considers additional measures for measuring the change in emissions of a company (as alternatives to absolute emissions or emissions intensity), such as using evidence of "*the existence of a credible plan to reduce the emissions in the future*". It suggests that this could take into account whether the company: (1) has emissions targets; (2) the percentage reduction in emissions; and (3) the duration of the target.
30. We consider that there are significant problems with relying on emissions targets to demonstrate that companies have reduced transition risk and, for many companies, this approach is likely to overstate the reduction in risk. This is because emissions targets may not be based on a credible and science-based transition plan. Companies can set unrealistic targets for 2030 or 2050 without adopting any transition plan to achieve those targets, and may rely on carbon offsets instead of reducing actual emissions.²³ In addition, companies that set emissions targets may nevertheless adopt business strategies that are inconsistent with science-based pathways to net-zero emissions, such as fossil fuel companies that engage in New Fossil Fuel Activities and/or do not have plans to phase out fossil fuel production in line with climate science (such as the IEA's net-zero pathway). For example,

by Thomas Buberl (CEO of AXA) that a world warmed by 4°C is "*not insurable*" (One Planet Summit – CEO speech in 2017), and by Jacki Johnson (at the time Group Executive for People, Performance and Reputation at IAG) that 4°C warming entails that "*the world becomes pretty much uninsurable*" (reported in the Australian Financial Review in 2018). See also 'Bank for International Settlements, 'The Green Swan: Central banking and financial stability in the age of climate change' (2020) which warns that unmitigated climate change would lead to a systemic financial crisis affecting the financial health of the insurance sector, which would render climate risks uninsurable.

²² See Network for Greening the Financial System, 'Technical supplement to the First NGFS Comprehensive Report' (2019), Mercer, 'Investing In A Time Of Climate Change — The Sequel' (2019) which finds: "*for nearly all asset classes, regions and timeframes, a 2°C scenario leads to enhanced projected returns versus 3°C or 4°C and therefore a better outcome for investors*", Swiss Re, 'The economics of climate change: no action not an option' (2021) which finds that global GDP could be 10% lower if the Paris Goals are not met.

²³ For an explanation of why carbon offsets are not a valid or effective means of achieving climate goals, see Fossielvrij NL writ in the claim *Fossielvrij NL v. KLM* at page 33.

TotalEnergies has targets to reduce emissions (compared to 2015) levels by 2030 and achieve net-zero emissions by 2050,²⁴ but its business strategy involves continued exploration for new oil and gas fields, and its targets rely on the use of forest-based carbon credits to purportedly offset its scopes 1 and 2 emissions for its 2030 target.²⁵

31. Even where companies do adopt transition plans, there are currently no clear legal requirements for the content or ambition of such transition plans, and so the plans may be unrealistic or not credible. Whilst some companies' emissions targets will be made in good faith with credible plans to achieve them, some in reality amount to little more than greenwashing. For example, Carbon Market Watch has reviewed 24 major companies' climate pledges and identified widespread bad practice in setting targets and disclosing plans for achieving emissions reductions, finding that *"Only three companies outline detailed information on their reduction measures"* and *"Most companies focus on efficiency improvements or present innovations that address just a small share of their emissions"*.²⁶ It concluded that the climate strategies of 15 of the 24 companies surveyed were of low or very low integrity, and that *"their combined emission reduction commitments are wholly insufficient to align with 1.5°C-compatible decarbonisation trajectories; targets and potential offsetting plans remain ambiguous; and the exclusion of emission scopes severely undermines the targets of several companies."* In addition, a report by CDP found that only 2% of companies which claimed to have adopted climate transition plans had actually disclosed sufficient details about those plans.²⁷ As a result, there is an inherent risk that the approach considered in the DP would give undue weight to unrealistic emission targets.
32. Accordingly, we suggest that EIOPA should be cautious in relying on the existence of forward-looking emissions targets in its transition risk exposure analysis or in a new dedicated prudential regime for transition risk exposures, and should ensure that they are not given more weight than is justified. The DP considers also relying on *"firm's success in reducing emissions in the past"* and its current emissions (absolute or intensity). We suggest that such data on past and current performance may be a more reliable indicator of transition risk. We note that the European Central Bank has adopted measures for assessing the degree of transition risk in corporate bond purchases, which combines data on past emissions, forward-looking emissions targets and climate disclosures,²⁸ which may be informative for EIOPA in developing its regime.

²⁴ See [TotalEnergies' website](#) on its net-zero targets.

²⁵ For further details, see [Greenpeace France's Summons](#) for the claim *Greenpeace France and others v TotalEnergies* at pages 41-42 and 46-47 (in relation to continued exploration) and page 45 (in relation to offsets).

²⁶ Carbon Market Watch, *'Corporate Climate Responsibility Monitor 2023'* (February 2023). See in particular: the key insights at page 5; section 2.1 at page 26; and section 3.1 at page 37.

²⁷ CDP, *'Are Companies Developing Credible Climate Transition Plans'* (February 2023). Over 18,600 companies responded to CDP's 2022 climate change questionnaire, of which 4,100 disclosed that they had already developed a 1.5°C-aligned climate transition plan. Of those 4,100, CDP found that only 81 (representing 2%) reported in sufficient detail against the 21 key indicators in CDP's climate questionnaire that align with a credible transition plan. See also Climate Action 100+, *'Net Zero Company Benchmark: Interim Assessments'* (October 2022) which found that *"the encouraging uptake of net zero commitments is not matched by the development and implementation of credible decarbonisation strategies"* and that *"While over half (53%) of focus companies have set short-term targets, only 10% of companies have short-term targets aligned with 1.5°C in 2025 that cover all material scopes of emissions"*.

²⁸ ECB, *'Press release: ECB provides details on how it aims to decarbonise its corporate bond holdings'* (19 September 2022); ECB, *'FAQ on incorporating climate change considerations into corporate bond purchases'* (October 2022); ECB, *'ECB decides on detailed modalities for reducing asset purchase programme holdings'* (2 February 2023).

33. We also have concerns that the DP's three proposed measures for assessing the ambition of emissions targets (summarised above) omit some relevant factors:

- a. The measures do not assess whether the emissions targets covers all of the company's emissions. Emissions targets often exclude key sources of emissions (for example, excluding scope 3 emissions, or excluding emissions from certain parts of the business). In some cases, the excluded emissions may be the most significant source of emissions for the company. For example, BP's absolute emissions reduction targets exclude the majority of its sold products, specifically excluding 'trading' sales (sales of products produced by third parties and bought and subsequently sold by BP) and unrefined crude oil sales. This means that BP's absolute emission reduction targets address only an estimated 17% of its total emissions.²⁹
- b. The measures do not assess whether the emissions targets are consistent with sectoral decarbonisation pathways. Certain sectors (e.g. fossil fuel extraction) need to decarbonize more quickly. Companies with emissions reduction targets that are not aligned with their sectoral decarbonization pathways will be exposed to transition risk.

Q16: Do you agree with focusing on greenhouse gas (GHG) emission intensities rather than on absolute GHG emissions? What is your view regarding the scope of emissions to be used (1, 2 or 3)?

34. The DP proposes relying on emissions intensity. We consider that EIOPA should also use information on absolute emissions, as companies need to manage their absolute emissions in order to mitigate their transition risk. In particular, in certain circumstances companies' emissions intensity will not be an effective proxy for their climate risk management, and emissions intensity may in fact reduce whilst the company's climate risks increase. For example, fossil fuel companies that engage in New Fossil Fuel Activities and expand their fossil fuel production will increase their absolute emissions in a manner that is inconsistent with global climate goals, which therefore exposes the company to significant transition risk (as set out in our response to question 13 above). However, such companies' emissions intensity could reduce if they (for example) reduce emissions from flaring methane, which would give a misleading impression of the company's overall climate risk management.

35. In addition, any measure of company emissions (whether intensity or absolute) used in EIOPA's transition risk exposure analysis or in new capital requirements should include scope 3 emissions. This is because:

- a. Scope 3 emissions are a vital component of many companies' emissions footprint, and therefore their transition risk. The Science Based Targets Initiative has found (in a survey of approximately 230 organisations) that, on average, scope 3 emissions represent over 70% of corporate emissions.³⁰ In many sectors, scope 3 emissions are the largest source of emissions.

²⁹ Global Climate Insights, 'BP GHG Emissions' (March 2022) at pages 3 and 8.

³⁰ SBTi, '[Scope 3: Stepping up science-based action](#)' (20 February 2023).

For example in fossil fuel activities, the vast majority of emission arise from the consumption of the fuel.³¹

- b. Data on scope 3 emissions is now more widely available, and EU and international standards are increasingly recognising that scope 3 emissions must be disclosed. For example: (1) the draft European Sustainability Reporting Standards require entities to disclose scope 3 emissions, and state that “*for many undertakings, Scope 3 GHG emissions may be the main component of the GHG inventory and are an important driver of the undertaking’s transition risks*”;³² the UN High Level Expert Group on the Net Zero Emissions Commitments of Non-State Entities’ recommendations state that net zero targets “*must include emissions reductions from a non-state actor’s full value chain and activities*” and that “*where data is missing for scope 3 emissions, businesses should explain how they are working to get the data or what estimates they are using*”;³³ and the Task Force on Climate-Related Disclosures’ updated Annex now “*strongly encourages all organizations to disclose Scope 3 GHG emissions.*”³⁴

36. We recognise that information on scope 3 emissions is not available for all companies. However, data gaps and challenges should not be used as a reason to adopt an approach to capital requirements that underestimates transition risk. For example, information on scope 3 emissions could be included where the information is disclosed by the relevant company and, where such information is not available, a method could be developed for estimating the scope 3 emissions (such as basing estimates on an assumed ratio of scopes 1 and 2 to scope 3 emissions for particular sectors). This is particularly important for sectors and organisations in respect of which scope 3 emissions are the most significant source of emissions (such as fossil fuels).

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³¹ CDP has found that for CDP survey respondents operating in the oil and gas sector, Scope 3 emissions from the “use of sold products” comprised 81% of total Scope 1-3 emissions. See CDP, ‘[Technical Note: Relevance of Scope 3 Categories by Sector](#)’ (April 2022) at pages 37-39.

³² EFRAG, ‘[Draft European Sustainability Reporting Standards: ESRS E1 Climate Change](#)’. See Disclosure Requirement E1-6 at page 11.

³³ UN HLEG, ‘[Integrity Matters: Net Zero Commitments by Businesses, Financial Institutions, Cities and Regions](#)’ (November 2022) at page 17.

³⁴ TCFD, ‘[Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures](#)’ (October 2021), see Recommended Disclosure 4(b) at page 21.